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DEFENSE ACQUISITION PROCESS

HEARINGS

BEFORE THE

COMMITTEE ON ARMED SERVICES
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

SECOND SESSION

JULY 11, 12, 27; AUGUST 4, 1988

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DEFENSE ACQUISITION PROCESS

MONDAY, JULY 11, 1988

U.S. SENATE,
COMMITTEE ON ARMED SERVICES,
Washington, DC.

The committee met, pursuant to notice, at 2:34 p.m., in room SR-222, Russell Senate Office Building, Senator Sam Nunn (chairman) presiding.

Present: Senators Nunn, Exon, Levin, Bingaman, Dixon, Shelby, Warner, Thurmond, Cohen, Quayle, Wilson, Gramm, and McCain.

Staff present: Arnold Punaro, staff director; Carl M. Smith, staff director for the minority; Romie L. Brownlee, deputy staff director; Jeffrey H. Smith, general counsel; Patrick A. Tucker, minority counsel; Andrew S. Effron, counsel; Gerald K. Bankus, Robert E. Bayer, Jonathan L. Etherton, Sherri Wasserman Goodman, John J. Hamre, George K. Johnson, Jr., Ronald P. Kelly, James P. Locher III, Patricia L. Watson, professional staff members; Tiffany E. Berger, Barbara L. Braucht, Pamela G. Powell, staff assistants; Melissa A. Ramsey, receptionist.

Also present: Jeffrey B. Subko, assistant to Senator Exon; Gregory J. Weaver and Peter K. Levine, assistants to Senator Levin; William J. Lynn, assistant to Senator Kennedy; Edward McGaffigan, Jr., assistant to Senator Bingaman; Charles C. Smith, assistant to Senator Dixon; Milton D. Beach and Donald A. Mitchell, assistants to Senator Glenn; Leon Fuerth, assistant to Senator Gore; Robert K. Griffith, assistant to Senator Wirth; Terrence Lynch, assistant to Senator Shelby; Dale F. Gerry, assistant to Senator Cohen; Henry D. Sokolski, assistant to Senator Quayle; Mark J. Albrecht, assistant to Senator Wilson; and Anthony H. Cordesman, assistant to Senator McCain.

OPENING STATEMENT OF SENATOR SAM NUNN, CHAIRMAN

Chairman NUNN. Today the committee begins a series of hearings on the defense acquisition system. Two years ago the Packard Commission diagnosed the acquisition system as "fundamentally ill." The recent allegations of fraud in DOD's source selection procedures indicate that the commission's diagnosis may have been too optimistic. There is a concern that a dangerous cancer may have taken root in the system.

But before we engage in radical surgery, we must properly diagnose the sources of the cancer and whether there are other diseases present in addition to the ones that we are concentrating on now. Otherwise we may inadvertently administer medicine that increases the patient's suffering without curing the underlying illness.

It is public knowledge that the investigations are at a very early stage. Vast quantities of documents have yet to be analyzed. Only a small number of interviews have been conducted, and no indictments have been returned. I think we should bear that in mind. It is important that these investigations be allowed to proceed without interference from either the executive or legislative branches. The committee intends to conduct our hearings in a manner that does not interfere with the investigations or any subsequent prosecutions or administrative actions.

It is also important that we place the current allegations of fraud within the context of other problems in the acquisition system. Fraud is not the only problem and, indeed, it may not be the most serious problem. Our committee has been particularly concerned over the years about the inability of the acquisition system to provide our men and women in uniform with quality equipment on a timely and cost effective basis. Just a few examples.

During the past 3 years, the Soviet Union has dramatically eroded the capability of NATO's antitank weapons by installing reactive armor on its tanks. Although reactive armor was invented in the United States nearly 18 years ago, our Army has ignored this capability until quite recently.

Another example. The average military production line is running at less than half of production capacity. Billions are being wasted on excess overhead because we rarely buy weapons systems at the production rate forecast at the outset of the program.

Another example. The average major acquisition program is 3 years behind in schedule in production, and that doesn't count the 12 to 15 years it take to develop a new weapon. We spend billions of dollars developing new capabilities, but many times we dissipate that investment by the lengthy development process followed by stretching out the production rates.

The concerns about fraud and corruption cannot and should not be minimized, but the above concerns are also serious and have an adverse impact on the process and on our defense capabilities. So, we will need to explore not only questions of fraud but the broader questions that also concern us greatly. We will need to ask questions such as:

Do the problems in our acquisition system reflect deficiencies in laws and regulations or weaknesses in the organization, management and oversight of the process?

Is the executive branch properly organized to deter, detect, investigate and prosecute fraud?

What points in the competitive source selection process are particularly vulnerable to fraud?

What are the consequences of abusing the source selection process in terms of price, quality and capability of major weapon systems?

What remedies are available to both the Government and disappointed offerors in the event of fraud in the source selection process?

What is the effect of such remedies on the timely delivery of weapons systems to the field? What is the effect of the revolving door on the integrity of the acquisition process?

What is the effect of the revolving door conflict of interest in dual compensation laws on the quality of the Government's acquisition work force?

And finally, what is the role of Congress in all of this? Do we need to pass new laws or have we passed too many laws already? We need to take a close look at our own role in terms of laws that are on the books, as well as proposals for the future, and oversight as well.

Finally, the hearing should provide a basis for assessing legislative or regulatory proposals directed at changing the system. As concrete proposals emerge, we will rely heavily on the expertise of Senator Jeff Bingaman's Subcommittee on Defense Industry and Technology to provide us with recommendations on any proposed changes. Senator Bingaman and Senator Gramm and others have been involved in this process for a long time, and we will be asking their opinion as we go forward.

This week we will be hearing from two distinguished witnesses. Today our witness will be Charles A. Bowsher, Comptroller General of the United States. Tomorrow morning we will hear from Secretary of Defense Carlucci. Mr. Bowsher will provide us with an overview of the acquisition process, focusing on the issues raised by the current allegations. We look forward to Mr. Bowsher's candid and forthright testimony reflecting not only the formal work of the GAO, but also his personal views based on his distinguished record in both the public and the private sectors.

Before turning to our witnesses today, I first ask Senator Warner for any comments he may have.

Senator **Warner**. Thank you, Mr. Chairman and members of the committee.

First I would ask that the Chair and the members of the committee unanimously request that a brief article on behalf of Richard J. Keegan be inserted in today's record. As you may recall, Mr. Keegan was a staff member on the Republican side at the time when we had the opportunity to chair this committee, and he made many useful contributions. And it is ironic that his contributions are primarily in the area that we are now examining in this hearing.

Chairman **Nunn**. Without objection.

[The article referred to follows:]

RICHARD J. KEEGAN, GOVERNMENT PROCUREMENT OFFICER

Richard J. Keegan, 59, a lawyer by training who was a former deputy assistant secretary of the Air Force and who also had worked for the Senate Armed Services Committee, died July 8 at Providence Hospital. He had cancer.

He was deputy assistant secretary of the Air Force for installations and logistics from 1972 to 1978. During those years, he had worked on the F-16 fighter project.

Mr. Keegan, who lived in Hyattsville, was a native of Brooklyn, N.Y. He was a 1951 graduate of the U.S. Naval Academy at Annapolis and received a law degree from Georgetown University in 1959.

He retired from active Navy duty in 1955, and for the next five years worked on patent and trademark projects with the Navy Department. He then transferred to the National Aeronautics and Space Administration, where he did procurement work, until 1972. He practiced law in Hyattsville from 1978 to 1986. He then joined the Armed Services Committee staff, where he worked until retiring for health reasons in 1987.

He was a member of several bar groups and of the Optimists Club.

Survivors include his wife, Eleanore Louise Keegan of Hyattsville; three daughters, Sarah Keegan of Washington, Mary Catherine Keegan-Ayer of Alexandria, and Elizabeth Keegan of Hyattsville; two sons, Richard Jr., of Davidsonville, Md., and James, of Laurel; a sister, Mary Louise Keegan of Brooklyn, and a grandchild.

KEEGAN, RICHARD Jr., on Friday, July 8, 1988, of Hyattsville, Md.; beloved husband of Eleanore Louise Keegan; father of Sarah G. Keegan, Richard Keegan Jr., Mary Catherine Keegan Ayer, James P., Elizabeth A. Keegan, brother of Mary Louise Keegan; grandfather of Haveril Keegan. Mr. Keegan will lie in state at St. Marks Catholic Church, 7501 Adelphi Rd., Hyattsville, Md., Monday, 2 to 4 and 7 to 9 p.m. Vigil prayers at 7:30 p.m., where Mass of Christian Burial will be on Tuesday, July 12 at 10 a.m. Interment Sacred Heart Cemetery, Bushwood, Md. The family suggest contributions to the P.G. County Chapter-American Cancer Society or American Red Cross. Arrangements by Hines-Rinaldi Funeral Home, Silver Spring, Md.

Senator WARNER. Mr. Chairman, I join with you in the importance of beginning these hearings on the defense acquisition process, and I draw to the attention of the members of the committee a release that you and I prepared in which we said that these hearings are to be conducted in a manner which in no way will interfere with the ongoing investigation by the Department of Justice and more particularly the U.S. Attorney's Office. In the request for witnesses—such documentation as we may require for this hearing—the chairman and myself and I am certain all members of the committee and the staff will work in such a way as not to interfere with those hearings.

Now, with respect to the public allegations, we must, I think, all avoid rushing to judgment before the facts are in on this very complicated case. This hearing and the one scheduled for tomorrow morning with Secretary Carlucci will help us build a record on the workings of the current acquisition system. As the facts in the investigations are made public, we will be in a far better position to assess whether changes to the organization or the process are appropriate. I believe that any effort to make legislative changes before that point could be premature.

The initial reports on this procurement problem have pointed to the actions of a few individuals, largely in one military department. We cannot afford to lose sight of the integrity of the vast majority of the tens of thousands of public servants and, indeed, those in the private sector who are working as we are sitting here this very moment to make the defense acquisition process bring the best possible product at the lowest possible price, in most instances, to our Government. We must be very mindful of the impact of any statement or contemplated action on the morale of this critical work force both in government and out of government.

In 1986, the President's Commission on Defense Management chaired by David Packard made comprehensive recommendations for improving the defense acquisition system. Both Congress and the Department of Defense have moved to implement the majority of these recommendations. Questions remain on the extent to which these changes to the organization in the process have really taken hold and address the fundamental ills diagnosed in the Commission's report.

During the course of our oversight of the acquisition process, we must also review the impact of the unprecedented volume of reform legislation passed by the Congress independently in the last 4 years. We need to determine whether this legislation has created or contributed in any way to the environment which apparently allowed this alleged fraud to take place and that encourages individuals in industry or the Department of Defense to engage in improper or alleged illegal conduct.

The Comptroller General of the United States is an appropriate witness for the first hearing in this series. The General Accounting Office has long been dedicated to investigating the deficiencies in the defense acquisition process. Mr. Bowsher is eminently qualified, and I have been privileged to know him and work with him for many, many years.

Thank you, Mr. Chairman.

Chairman **Nunn**. Thank you very much, Senator Warner.

Mr. Bowsher, we are delighted to have you here today.

And I might say that this committee, certainly as Senator Warner has said and I said in my opening statement, does not intend to get into the investigative aspects of this overall matter. We do intend to concentrate on policy. We do not intend to get into any rush. I don't think we are going to rush out and cure these problems overnight. I believe we are going to have to take our time, and we're going to have to go into this with a degree of thoroughness and care so that we at least mitigate the problems rather than making them worse.

Mr. Bowsher, we are delighted to have you. Why don't you proceed?

Senator **Thurmond**. Mr. Chairman, would you allow me to speak?

Chairman **Nunn**. I'd be glad to. Senator Thurmond.

Senator **Thurmond**. I have a few questions that if they could be asked for the record, I'd appreciate it.

Chairman **Nunn**. Delighted. They will be part of the record.

Mr. Bowsher, would you please proceed now.

STATEMENT OF HON. CHARLES A. BOWSHER, COMPTROLLER GENERAL OF THE UNITED STATES, ACCOMPANIED BY JAMES HINCHMAN, GENERAL COUNSEL; FRANK CONAHAN, ASSISTANT COMPTROLLER GENERAL FOR NATIONAL SECURITY, INTERNATIONAL AFFAIRS DIVISION

Mr. **Bowsher**. Thank you, Mr. Chairman, and members of the committee. We are pleased to be here today, and we appreciate the opportunity to comment as you consider what action is necessary to deal with the events related to the investigations at the Department of Defense.

First, I think it might be useful to step back and look at the environment in which defense procurement takes place. Then I would like to discuss several areas where improvements might possibly be made.

I have always supported a strong national defense, but for several years I have been expressing concerns about the potential consequences of an uncontrolled, rapid defense build-up. As we look at the history of the defense procurement since the 1940s we see the same recurring problems accompanying these very rapid defense expansions. We had procurement scandals during World War II, the Korean war and then again now here in the last few years, all during periods of rapid growth in defense spending. The fact that we are having procurement problems today does not necessarily mean that we have not made progress. Rather it is testimony to the fact that Government oversight and management attention, including management attention in the private sector, on a continuing basis is essential.

In addition to these scandals, I think the other shoe will probably fall soon, namely, many big cost overruns. I suspect the Stealth airplane program, the Navy shipbuilding program and other programs which have to be stretched because of budget constraints will all result in very large cost increases that the Congress and the taxpayer will have to finance.

Before dealing with internal controls, disclosure and those matters that more directly relate to the defense fraud, I would like to briefly discuss a number of troublesome areas that affect the procurement process.

Since the mid-1960s, the DOD budget has never really had an extended period of stability. Rather, we see periods of rapid growth followed by periods of austerity followed by rapid growth again. This cycle inhibits managers within the Department from making sound management decisions. It encourages managers to procure as much as possible when funding is relatively plentiful and not attempt to develop a stable and realistic procurement plan. I think that this is a major problem. History shows that when too much money is being pumped into the acquisition system over a relatively short period of time, we will have problems.

Over the next few years we will be facing some very difficult decisions involving defense spending. The Secretary, to his credit, has expressed a willingness as we enter a period of restrained defense spending to address these issues. However, we believe that the services still have too many systems chasing too few dollars. Additional programs will have to be cut. In such an environment, we cannot afford either sloppy or corrupt practices.

More specifically we cannot afford to invest large sums of money in such programs as AQUILA and the DIVAD only to have them terminated. While we applaud the decisions to terminate these programs, they should not have progressed as far as they did in the acquisition process before being terminated. In addition, we cannot afford to allow inventories to exceed requirements by $20 billion, as happened in the depot level stocks between 1980 and 1987. Nor can we afford to allow repair parts inventories to become so big that they cannot be managed effectively as happened in Europe. Finally, we cannot afford to pay exorbitant prices for spare parts and equipment because the management focus is on the number of actions processed rather than the reasonableness of the prices paid. Again from my perspective, these are examples of what happens when too much funding is pumped into the system too quickly.

Another thing is clearly evident: we need to be realistic in projecting the quality, cost and schedule of our systems in relation to the state of the technology involved. We still are unable to get contractors to build things right the first time as clearly is obvious in the case of the B-1B program. It is clear to me that some of the things that went wrong on the B-1B included concurrency, inadequate testing, a push to deliver on time and at cost no matter what while stretching the state of technology. Until we do this better, we will continue to buy into programs which will not achieve their advertised performance capabilities and will continue to exacerbate the affordability issues.

Testing of our weapon systems ties directly with my concerns on quality. Our work has shown that during the later years of program development, weapons historically experience the significant cost growth and schedule slippages as technical and other problems surface. DOD's policy emphasizes the need for early testing to identify and reduce the acquisition risk of costly redesign and modification after deployment. We must perform these tests in a mode which ensures independence and a clear separation of involvement from contractors who have played key roles in the system's development.

As I reflect on my experience in the public and the private sectors, I become more and more convinced of the need to have first-rate people in key positions. The defense acquisition process is extremely complex and requires skills and knowledge that can only be developed over an extended period of time. Yet, frequently key acquisition positions are filled with people who are often unprepared for their assignments. While I believe that this is true at all levels, it is especially true at the program office level.

We have made some progress in this area. For example, the services, in response to congressional directives, changed the requirements for program managers and made the requirements more stringent. This is a start, but more is needed. We need to raise the status of these individuals in procurement. As I see it, we need to increase the professionalism of the procurement work force and in so doing, impart greater prestige to the individuals and compensate them accordingly.

Now, it is essential that we have full disclosure by DOD and industry regarding the procurement of goods and services. In the past years we created entities such as the Cost Accounting Standards Board to help achieve this. But the goals were never really fully achieved. This occurred in part because DOD and industry failed to provide sufficient support. It distresses me to see continuing resistance to such a concept.

Over the past several years there has been a continuing concern involving the reporting of contractor profit data, weapon system cost data as well as DOD and industry compliance with laws such as the Federal Managers' Financial Integrity Act and the Truth in Negotiations Act. The Congress and GAO have recognized the importance of internal management control systems and have encouraged improvements. Unfortunately, both industry and DOD have resisted many of the proposed improvements.

For example, in September 1986, we issued a report which proposed a program to study the profitability of Government contractors. Our proposal was designed to build upon and improve the methodology DOD used to perform its previous profit studies. Even though several pieces of legislation have been proposed to initiate such a program, segments of which are in the current defense authorization bill, DOD and industry opposition is so great that its enactment in a useful form is really questionable.

While the effectiveness of the Government's profit policy is important, most of the GAO's audit efforts over the past several years have focused on costs. In the 1960s the Congress passed two laws intended to ensure better information on contractor costs: Public Law 87-653, which is the Truth in Negotiations Act; and Public Law 91-379, which created the Cost Accounting Standards Board.

The Truth in Negotiations Act requires contractors to certify that their cost or pricing data used in negotiations is current, accurate and complete. Our work has consistently shown that contractor compliance with the act falls short of disclosure. Since 1986, we have issued 19 reports which reported on contractors' failures to fully disclose current, accurate and complete data.

Further, we have found problems in the systems contractors have used to develop these cost estimates. For example, some contractors did not have written estimating procedures for developing estimates and some have not adequately documented the methods and supporting data which were used to develop the estimates. In the absence of good estimating systems, contracts can be significantly overpriced.

I continue to believe that the cost accounting standards can be a significant aid in establishing the integrity and the credibility of cost data used by DOD and industry. Since the demise of the Cost Accounting Standards Board, there has been no governmental group to amend standards when desirable or to provide interpretations, waivers or exemptions to the standards. The capability to perform these functions needs to be established. Independence was one of the features sought in establishing the original board, and this should continue to be a primary feature for any group selected to assume these functions.

Even though the Government has mandated effective internal management controls for over 30 years, the increasing need for information about expanding Government activities necessitated that greater attention be directed at the effectiveness of internal controls. As a result, the Congress passed the Federal Managers' Financial Integrity Act which requires Government agencies to continuously evaluate their internal controls. The legislation contains a key feature to implement the internal control evaluation process. The head of each agency must submit an annual report to the President and the Congress that describes the internal control weaknesses and provides a schedule and plan for correcting the weaknesses.

Over the last several years, the internal management control program, which was implemented to comply with the Financial Integrity Act, has resulted in the identification and correction of a number of significant problems. However, we are concerned that the Department is often too reactive rather than proactive in implementing this program. Too often it seems DOD reports weaknesses only after they have been disclosed by others.

In one case having a direct bearing on what we are discussing today, the Commander of the Naval Security Investigative Command in October 1987 reported instances of procurement fraud, such as conflict of interest and bribery, and that several of the command's ongoing and recently closed investigations involved high ranking naval officers and high level Navy Department civilians. The Commander also said that such problems did not indicate that the internal control systems were flawed, but that emphasis must continue to be given to compliance with existing systems in assigning personnel responsibility for proper operations of those systems.

Reports such as the Commander's are provided from all levels within DOD, and the weaknesses deemed material are reported annually up to the Secretary of Defense and then to the Congress and then to the President. However, in the above case, we were told that in the review process it was decided that this was not a material or systematic weakness so it was not included in the Secretary of the Navy's report to the Secretary of Defense.

I think this is somewhat analogous to the reporting on weaknesses in DOD supply operations. Supply operations weaknesses have been around for years and reported at various levels within DOD. However, it was not reported by DOD as a material weakness until after your committee's Task Force on Military Inventory Management was formed to review the problems we were finding and reporting. I'm afraid that reporting on and dealing with procurement fraud will follow this same reactive scenario.

In testifying before the Packard Commission, I stated that the first line of defense in controlling fraud, waste and abuse is an adequate control system that is fully supported at all levels of a company. An adequate control system permits a company to institute preventive steps as opposed to reacting after the fact. Many defense contractors are subject to the provisions of the Securities and Exchange Act's recordkeeping and internal accounting control requirements.

The control provisions of that act requires that the company devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that certain specified objectives are attained. However, the act's control and reporting provisions do not specifically cover cost, price, estimates, billing and performance measurement controls, nor do they report on such controls. However, I am able to report that the SEC just this past week began to address some of these provisions.

A recent initiative flowing out of the Packard Commission and being advanced by DOD is Contractor Self-Governance. This concept deals with the responsibility and accountability of top management to assure that defense work is performed in compliance with procurement laws and regulations and is subject to high ethical standards. While I agree that the concept must be developed, I am also discouraged, as was the DOD Inspector General who testified before the House Armed Services Committee last week, that only 46 contractors have signed on to this initiative. I believe that it is time to seriously consider legislation which would require an annual management report on the controls and an independent public accountant's opinion on the management's representation.

I think that it is important to note that over the past 6 months support for less oversight over the defense industry was building. And some of the initiatives I've discussed begin to open a door for greater reliance on the integrity of the defense contractors. James Forrestal, the first Secretary of Defense, saw opportunities for maintaining an effective working relationship between industry and Government. Yet, as we face the problems of today, I cannot think of a more appropriate time to reexamine this relationship and to make it work better. In that regard, we must keep vigilant oversight to assure that industry institutes the needed control measures.

No matter how many and what type of controls are in place, you are still going to have compliance problems, and these have to be dealt with to the full extent of the law. The Attorney General has given a number of crime areas high enforcement prosecution priority. These include organized crime as well as white collar crime. The investigation of defense procurement fraud is a top priority in the white collar crime area. Despite this, the Justice Department's overall management of its defense procurement fraud investigations could be improved. The Attorney General does not have complete or timely information on a significant number of defense procurement fraud referrals, and does not know the amount of attorney resources spent in this effort.

Neither the criminal division nor the U.S. Attorney's offices have developed written plans that identify their defense procurement fraud efforts and allow comparison of planned with actual accomplishments. Officials from both units say that they need additional resources, both attorneys and support staff, to handle the defense procurement fraud cases, many of which are highly complex and time consuming. Justice does not have a system to help distinguish the different prosecutive efforts required for different types of cases. Better information could help the Department assess the extent to which this high priority program is using resources effectively and efficiently.

Mr. Chairman, there will be a tendency to seek fast remedies for the underlying causes of the recently reported abuses. While the criminal aspects of this investigation are decided within the judicial system, we should focus our attention on the needed controls and reporting. While some steps can be taken along the lines we have just discussed, we must make certain that any initiatives by the executive branch or the Congress are, in fact, the correct solutions to the problems.

There are two specific areas that we are presently examining. We are reviewing the organizational restructuring of the procurement process in DOD and the services that has taken place in the 1980s. We will focus on whether these changes resulted in the weakening of the internal controls which are needed to curb the type of abuses being reported. In addition, a careful review is needed on what actions are necessary in the consultant area. We will continue our work in this area with a detailed examination of the role of consultants in the procurement process. This work will take into account the revolving door issue and how the spirit of the recent laws was avoided.

We will also continue to work with this committee and other committees in whatever further study is required into any of the issues that we've discussed today.

Mr. Chairman, that concludes our remarks. We'd be more than happy to answer any questions.

[The prepared statement of Mr. Bowsher follows:]

PREPARED STATEMENT OF CHARLES A. BOWSHER, COMPTROLLER GENERAL OF THE UNITED STATES

Mr. Chairman and members of the committee: I appreciate the opportunity to be here today as you consider what action is necessary to deal with the events related to the investigations at the Department of Defense. First, I think it might be useful to step back and look at the environment in which Defense procurement takes place. Then I would like to discuss several areas where improvements could be made.

I have always supported a strong national defense, but for several years I have been expressing concerns about the potential consequences of an uncontrolled rapid defense build up. As we look at the history of Defense procurement since the 1940s, we see the same recurring problems accompanying rapid Defense expansions. We had procurement scandals during World War II, the Korean War, and in the past few years—all during periods of rapid growth in defense spending. The fact that we are having procurement problems today does not necessarily mean that we have not made progress, rather it is testimony to the fact that government oversight and management attention on a continuing basis is essential.

In addition to these scandals, I think the other shoe will probably fall soon, namely, many big cost overruns. I suspect the Stealth airplane program, the Navy shipbuilding program, and the other programs which have to be stretched because of budget constraints will all result in very large cost increases that the Congress and the taxpayer will have to finance.

Before dealing with internal controls, disclosure and those matters that more directly relate to defense fraud, I would like to briefly discuss a number of troublesome areas that affect the procurement process.

THE PROCUREMENT ENVIRONMENT

Since the mid-sixties, the DOD budget has never had an extended period of stability. Rather we see periods of rapid growth followed by periods of austerity followed by rapid growth again. This cycle inhibits managers within the Department from making sound management decisions. It encourages managers to procure as much as possible when funding is relatively plentiful and not attempt to develop a stable and realistic procurement plan. I think that this is a major problem. History shows that when too much money is being pumped into the acquisition system over a relatively short period of time, we will have problems.

Over the next few years, we will be facing some very difficult decisions involving Defense spending. The Secretary, to his credit, has expressed a willingness, as we enter a period of restrained Defense spending to address these issues. However, we believe that the services still have too many systems chasing too few dollars. Additional programs will have to be cut. In such an environment we cannot afford either sloppy or corrupt practices.

More specifically, we cannot afford to invest large sums of money in such programs as AQUILA and DIVAD only to have them terminated. While we applaud the decisions to terminate these programs, they should not have progressed as far as they did in the acquisition process before being terminated. In addition, we cannot afford to allow inventories to exceed requirements by $20 billion as happened in depot level stocks between 1980 and 1987. Nor can we afford to allow repair parts inventories to become so big that they cannot be managed effectively as happened in Europe. Finally, we cannot afford to pay exorbitant prices for spare parts and equipment because the management focus is on the number of actions processed rather than the reasonableness of the prices paid. Again from my perspective, these are examples of what happens when too much funding is pumped into the system too quickly.

Another thing is clearly evident: we need to be realistic in projecting the quality, cost and schedule of our systems in relation to the state of the technology involved. We still are unable to get contractors to build things right the first time as is clearly obvious in the case of the B-1B program. It is clear to me that some of what went wrong on the B-1B included concurrency, inadequate testing, a push to deliver on time and at cost—no matter what, while stretching the state of technology. Until we do this better, we will continue to buy into programs which will not achieve their advertised performance capabilities and will continue to exacerbate the affordability issues.

Testing of our weapon systems ties directly with my concerns on quality. Our work has shown that during the later years of program development, weapons historically experience the significant cost growth and schedule slippages as technical and other problems surface. DOD's policy emphasizes the need for early testing to identify and reduce the acquisition risk of costly redesign and modification after deployment. We must perform these tests in a mode which ensures independence and a clear separation of involvement from contractors who have played key roles in a system's development.

As I reflect on my experience in the public and private sectors, I become more and more convinced of the need to have first rate people in key positions. The Defense acquisition process is extremely complex and requires skills and knowledge that can only be developed over an extended period of time. Yet frequently, key acquisition positions are filled with people who are often unprepared for their assignments. While I believe that this is true at all levels, it is especially true at the program office level.

We have made some progress in this area. For example, the services, in response to congressional directives, changed the requirements for program managers and made the requirements more stringent. This is a start, but more is needed. We need to raise the status of those individuals in procurement. As I see it, we need to increase the professionalism of the procurement work force and, in so doing, impart greater prestige to the individuals and compensate them accordingly.

CONTROLS AND BETTER DISCLOSURE NEEDED FOR THE PROCUREMENT PROCESS

It is essential that we have full disclosure by DOD and industry regarding the procurement of goods and services. In past years we created entities such as the Cost Accounting Standards Board to help achieve this, but the goals were never fully achieved. This occurred, in part, because DOD and industry failed to provide sufficient support. It distresses me to see continued resistance to such a concept.

Over the past several years there has been a continuing concern involving the reporting of contractor profit data, weapon system cost data as well as DOD and industry compliance with laws such as Federal Managers' Financial Integrity Act (FIA) and the Truth in Negotiations Act. The Congress and GAO have recognized the importance of internal management control systems and have encouraged improvements. Unfortunately, both industry and DOD have resisted many of the proposed improvements. For example, in September, 1986 we issued a report which proposed a program to study the profitability of government contractors. Our proposal was designed to build upon and improve the methodology DOD used to perform its previous profit studies. Even though several pieces of legislation have been proposed to initiate such a program, segments of which are in the current defense authorization bill, DOD and industry opposition is so great that its enactment in a useful form is questionable. While the effectiveness of the government's profit policy is important, most of GAO's audit efforts over the past several years have focused on costs. In the 1960s Congress passed two laws intended to ensure better information on contractor costs—Public Law 87-653 which is the Truth in Negotiations Act and Public Law 91-379 which created the Cost Accounting Standards Board.

The Truth in Negotiations Act requires contractors to certify that their cost or pricing data used in negotiations is current, accurate, and complete. Our work has consistently shown that contractor compliance with the Act falls short of full disclosure. Since 1986 we have issued 19 reports which reported on contractors' failures to fully disclose current, accurate and complete data. Further, we have found problems in the systems contractors have used to develop their cost estimates. For example, some contractors did not have written estimating procedures for developing estimates and some had not adequately documented the methods and supporting data which were used to develop the estimates. In the absence of good estimating systems, contracts can be significantly overpriced.

I continue to believe that the Cost Accounting Standards can be a significant aid in establishing the integrity and the credibility of cost data used by DOD and industry. Since the demise of the Cost Accounting Standards Board, there has been no governmental group to amend standards when desirable, or to provide interpretations, waivers, or exemptions to the standards. The capability to perform these functions needs to be established. Independence was one of the features sought in establishing the original Board and this should continue to be a primary feature for any group selected to assume these functions.

Even though the government has mandated effective internal management controls for over 30 years, the increasing need for information about expanding government activities necessitated that greater attention be directed at the effectiveness of internal controls. As a result, the Congress passed the Federal Managers' Financial Integrity Act which requires government agencies to continuously evaluate their internal controls. The legislation contains a key feature to implement the internal control evaluation process. The head of each agency must submit an annual report to the President and the Congress that describes the internal control weaknesses, and provides a schedule and plan for correcting the weaknesses.

Over the last several years the Internal Management Control Program which was implemented to comply with the Financial Integrity Act has resulted in the identification and correction of a number of significant problems. However, we are concerned that the Department is often too reactive rather than proactive in implementing this program. Too often, it seems, DOD reports weaknesses only after they have been disclosed by others. For example, in one case having a direct bearing on what we are discussing today, the Commander of the Naval Security and Investigative Command, in October 1987, reported instances of procurement fraud, such as conflict of interest and bribery, and that several of the Command's ongoing and recently closed investigations involved high ranking Naval officers and high level Navy Department civilians. The Commander also said that such problems did not indicate that the internal control systems were flawed but that emphasis must continue to be given to compliance with existing systems and assigning personnel responsibility for proper operation of those systems.

Reports, such as the commander's are provided from all levels within DOD and the weaknesses deemed material are reported annually up to the Secretary of Defense and then to the Congress and to the President. However, in the above case, we were told that in the review process it was decided that this was not a material or systemic weakness so it was not included in the Secretary of the Navy's report to the Secretary of Defense.

I think this is somewhat analogous to the reporting on weaknesses in DOD supply operations. Supply operations weaknesses have been around for years and reported at various levels within DOD. However, it was not reported by DOD as a material weakness until after your Committee's Task Force on Military Inventory Management was formed to review the problems we were finding and reporting. I am afraid that reporting on and dealing with procurement fraud will follow this same reactive scenario.

In testifying before the Packard Commission, I stated that the first line of defense in controlling fraud, waste and abuse is an adequate control system that is fully supported at all levels of a company. An adequate control system permits a company to institute preventive steps as opposed to reacting after the fact. Many Defense contractors are subject to the provisions of the Securities and Exchange Act's recordkeeping and internal accounting control requirements. The control provisions of the Act require that the company devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that certain specified objectives are attained. However, the Act's control and reporting provisions do not specifically cover cost, price, estimates, billing, and performance measurement controls nor do they report on such controls. Recent SEC initiatives, however, begin to address some of these provisions.

A recent initiative flowing out of the Packard Commission and being advanced by DOD is Contractor Self Governance. This concept deals with the responsibility and accountability of top management to assure that defense work is performed in compliance with procurement laws and regulations and is subject to high ethical standards. While I agree that the concept must be developed, I am also discouraged—as was the DOD IG who testified before the House Armed Services Committee last week—that only 46 contractors are signatories to this initiative. I believe that it is time to seriously consider legislation which would require an annual management report on the controls and an independent public accountant's opinion on management's representation.

I think that it is important to note that over the past six months support for less oversight over the defense industry was building. And some of the initiatives I have discussed begin to open a door for greater reliance on the integrity of defense contractors. James Forrestal, the first Secretary of Defense, saw opportunities for maintaining an effective working relationship between industry and government. Yet, as we face the problems of today, I cannot think of a more appropriate time to reexamine this relationship and make it work better. In that regard, we must keep vigilant oversight to assure that industry institutes needed internal control measures.

No matter how many and what type of controls are in place, you are still going to have compliance problems and these have to be dealt with to the full extent of the law. The Attorney General has given a number of crime areas high enforcement and prosecution priority. These include organized crime as well as white collar crime. The investigation of defense procurement fraud is a top priority in the white collar crime area. Despite this, the Justice Department's overall management of its defense procurement fraud investigations could be improved. The Attorney General does not have complete or timely information on a significant number of defense procurement fraud referrals and does not know the amount of attorney resources spent in the effort.

Neither the Criminal Division nor the U.S Attorney's offices have developed written plans that identify their defense procurement fraud efforts and allow comparison of planned with actual accomplishments. Officials from both units say that they need additional resources (both attorneys and support staff) to handle defense procurement fraud cases, many of which are highly complex and time consuming. Justice does not have a system to help distinguish the different prosecutive efforts required for different types of cases. Better information could help the Department assess the extent to which this high priority program is using resources effectively and efficiently.

Mr. Chairman, there will be a tendency by everyone to seek fast remedies for the underlying causes of the recently reported abuses. While the criminal aspects of this investigation are decided within the judicial system, we should focus our attention on the needed controls and reporting. While some steps can be taken along the lines we have just discussed, we must make certain that any initiatives by the executive branch and/or the Congress are, in fact, the correct solutions to the problems.

There are two specific areas that we are presently examining. We are reviewing the organizational restructuring of the procurement process in DOD and the services that has taken place in the 1980s. We will focus on whether those changes resulted in a weakening of the internal controls which are needed to curb the types of abuses being reported. In addition, a careful review is needed of what actions are necessary in the consultant area. We will continue our work in this area with a detailed examination of the role of consultants in the procurement process. This work will take into account the revolving door issue and how the spirit of the recent laws was avoided.

We will also continue to work with this committee and other committees in whatever further study is required into any of the issues I have discussed today.

That, Mr. Chairman, completes my prepared remarks. I would be happy to address any questions the committee may have at this time.

Chairman **Nunn**. Thank you very much, Mr. Bowsher.

Let me just start off with a question as to how the competitive process works today. If you could tell us how a competitive negotiation—let's say, you pick out any hypothetical contract you like or any actual contract. Without any bearing on the fraud, just how does this system work today?

Mr. **Bowsher**. Well, it varies somewhat by the different weapon systems, but an overall description I think would be that an RFP—that is, a request for a proposal—is sent out. Sometimes before an RFP is sent out, specifications are drawn up and sometimes industry people are consulted. Lots of times industry has to be consulted to get some technical input on certain matters. Then the RFP goes out and industry responds.

When the responses come in, a selection can be made, but many times a selection is not made then. Actually you go into negotiation with individual contractors. In other words, the negotiations are the Government talking to the individual contractor.

And then you get another round of offers which are known as the best and final offers. You can go around that more than once.

And then, finally, a source selection authority, used generally on the big procurements with a source selection advisory board to help him make the final determination as to who wins the contract.

Chairman NUNN. Now, when the contractors submit their first proposal based on the first request for proposal, RFP, they submit their own ideas about how that particular weapon system should work. Is that right?

Mr. BOWSHER. That's right.

Chairman NUNN. A lot of discretion in there.

Mr. BOWSHER. Yes.

Chairman NUNN. A lot of differences.

To whom does that data belong? I'm a contractor A. You've asked me to give you a proposal to, let's say, take an airplane full of equipment from the supply lines to the forward battle area. I make you a proposal giving you, let's say, a heavy lift helicopter. Another contractor says, no, I can do it better with a small twin engine aircraft, and they both have varying differences in their proposal. Who owns that data at that stage and what can the Government do with that data?

Mr. BOWSHER. The contractor owns the data and especially the proprietary features of it. In other words, as you point out, some of these can vary from one contractor to another. They have different solutions as to how the weapons should be developed. And so, that's what they have proposed, and that proposal frequently contains proprietary data.

Chairman NUNN. Let's say that contractor A has certain things that are good in that proposal. Contractor B has certain things the Government likes in that proposal. They decide to take the best features of both and merge them into a new request for proposal and send that out. Is that permissible for the Government to do?

Mr. BOWSHER. Yes, it is, provided the Government acquires data right from both contractors.

Chairman NUNN. Now, that's sharing contractor A's information with the contractor B, is it not?

Mr. BOWSHER. But when you share it, you have to share with everybody. In other words, you just don't do it with contractor A and B. Whenever they go out for a resubmission, at that point everybody gets another crack at the submission.

Chairman NUNN. So, it's understood when contractor A submits their proposal, that that data can be used by the Government. That's part of the deal. It can be used by the Government in developing a subsequent RFP. Is that right?

Mr. BOWSHER. That's right, but only if the Government acquires rights to the data. Lots of time industry would prefer that it not be done that way, but if the Government has acquired rights to the data, the Government has the right to do it that way.

Chairman NUNN. All right. Now, we hear a lot about the best and final offer. Tell us what that means.

Mr. BOWSHER. Well, the best and final offer is when you are asking the contractors to come back and give not only their final price, but also their best offer as to what would be offered.

Chairman NUNN. Is that supposed to be the last bid?

Mr. BOWSHER. That's supposed to be the last bid but, as I say, you can recycle that and go around again.

Chairman NUNN. Isn't it happening more and more that the best and final offer is not the best and final offer, but simply the first of several of those kind of similar steps?

Mr. **Bowsher**. I'm not sure what the numbers are and we would have to do some additional review to determine them. But for some time, there has been more than one best and final offer on many of these weapon systems.

Chairman **Nunn**. It seems to me that raises some real questions at that stage whether that's misleading in itself when one contractor may believe that it's the best and final offer and others may simply still be in the game playing stage. How in the world do you control a process when you call something the best and final offer and then it goes around several times?

Mr. **Bowsher**. I think that this is one feature of the Government procurement process that industry has found troublesome over the years. No question about it.

Chairman **Nunn**. I'm just wondering if that has some incentive for some of the things we've seen transpire, at least in the form of allegations.

Let me ask you another question. You've cited, going back to World War II and probably even before, all sorts of procurement scandals we've had with the defense area. Is there anything that distinguishes this one from those in the past, or is this just another go-around? I'm simply asking you to reflect based on the allegations you've read and nothing inside.

Mr. **Bowsher**. Yes. And that's right. All we know is the allegations that we have seen in the press.

The one thing that I think that distinguishes this one possibly is that it is fairly high up. In other words, in the private sector, we often distinguish between regular or normal fraud—workers mischarging time cards and things like that down in the plant—versus management fraud. Management fraud is much harder to detect especially by normal reviews because that means the top people are involved. I think the thing that discouraged me most about this set of allegations is that it seems as if some very senior people might be involved.

Chairman **Nunn**. Would you agree that actually the number of people involved here may not indicate the depth since one or two individuals, possibly because they might be high level, could have affected scores and scores of contracts?

Mr. **Bowsher**. I think that's a real possibility.

Chairman **Nunn**. One other question and then I'll defer to Senator Warner.

Do you have any observations about what procedure should be followed in terms of the Department of Defense and/or the Congress deciding to set aside existing contracts because of taint, fraud? In other words, is there a procedure that you would suggest?

Mr. **Bowsher**. I would suggest not rushing on that area. In other words, you have suspension and debarment procedures. You have bid protest procedures. I think it might be better to let the investigative process work, and see just what the situation is, before taking any unusual steps, you might say, on individual contracts.

I think at some point in time if it is indicated that people are being indicted, then I think you have to look at the suspension rules and maybe suspend some of the contractors. I think if there are convictions, I think you have to look for debarments.

So, I would be more inclined to recommend much in the spirit of your opening statement that the existing laws and regulations on the individual—it might be better to let that work as the laws now stand.

Chairman NUNN. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman. Well, let me just pick up on that.

One of the major issues in the investigation appears to be the security of sensitive data in the source selection process touched on by the chairman. The regulations and the instructions issued by each of the services are fairly explicit about the needs to secure source selection sensitive data at each stage of the process. Do you have any information on the effectiveness of these procedures and what additional actions would you recommend?

Mr. BOWSHER. As I said in the latter part of my statement that's an area that we are currently studying. We would hope to have a report for the Congress in a few months. The thing that worries me most, Senator Warner, is that possibly in some of the reorganization that took place over in the Defense Department, some of the key control features might have been taken out of place so that a few individuals got more control over the levers of decisionmaking than what they possibly had in the past.

When you look at the regulations, when you look at the rules, you have a sense that they are pretty thorough, that they are pretty good. But, obviously, some problems have occurred that need a new look. I just have a suspicion that some of the key controls of the past were amended, changed, even done away with.

If I could just use one example. If you remember when we had the Naval Material Command, we had a contract review function——

Senator WARNER. Which I think for the record we should indicate it now ceases to exist.

Mr. BOWSHER. It now ceases to exist. That was done as part of a reorganization.

Senator WARNER. By Secretary Lehman.

Mr. BOWSHER. By Secretary Lehman.

All right. Now, if you remember, we had a final procurement review function in that Command that was headed by Captain Doc Freeman for many years and Gordon Rule. Therefore, whatever the procurement process was going on had to go through that hurdle. I'm not sure that that hurdle is still there.

I am also surprised, to be honest with you, as I read the counts here, that the Assistant Secretary for R&D can have that much control, that much influence.

Senator WARNER. Mr. Bowsher, let's identify the military department.

Mr. BOWSHER. For the Navy.

Senator WARNER. The Navy.

Mr. BOWSHER. That the Assistant Secretary for R&D in the Navy can have that much control and influence over the acquisitions. It was not that way in the past. And so, that's what I would like to examine—have some teams thoroughly review the situation and report back to the committee as to what got changed, and what allowed some of this to happen.

Chairman **Nunn**. Why don't you consider yourself under request to make the kind of examination and report.

Mr. **Bowsher**. All right. We'd be pleased to accept that.

Senator **Warner**. Mr. Chairman, that brings me to my next observation, and I'll put it in the form of a question. As the facts begin to come forth in this instant case—and I'm not sure that I quantify it accurately, but certainly within the ballpark—it appears to be the vast majority in one military department, i.e., the Navy; some in the Department of Air Force and thus far minimal in the Department of the Army.

Now, your statement didn't distinguish. Your statement was a fairly sweeping indictment of the whole system. Should we not wait until we determine if there were not certain procedures, changes, organizational, otherwise in the Department of the Navy which might have fostered this problem which were not present in the other military departments before we leap to change?

Mr. **Bowsher**. I agree. We should not make changes unless we are certain of them. But I think it's worth looking at all three services. I think you could have a situation in one of the services where you had a person of high integrity that didn't allow anything to happen, but maybe you set up the potential, just as you did in the service where it did happen. I think we should review all three and report. I think you might find that maybe everything is okay in one or two of the services. But I think we should look at all three and their relationship.

One of the other things that changed, when compared to the previous administration, was when they took away the fourth Assistant Secretary in the services. They allowed the services to organize the way they wanted. You got a real mixture of organization at what I call the appointee level, the Assistant Secretary level, and you gave up what I think was at one time a very strong part of the defense organization, and that was the mirror organization. For example, you had the R&D chain, the controller chain, the I&L chain. And we gave that up in the late 1970s, and that allowed people to organize in different ways, I suspect people made some changes at that point too that should be looked at very carefully.

Senator **Warner**. Are you at all concerned about the volume of laws that Congress has enacted in this area recently that might be a contributory factor?

Mr. **Bowsher**. Yes. I think that we should not jump to any conclusions such as, we need more laws, more regulation, more redtape, but at the same time, something broke down, and I think we have got to take a hard look at it. We might be better off having fewer laws and regulations, if we could effectively monitor them and enforce them.

Senator **Warner**. My time is up, Mr. Chairman.

Chairman **Nunn**. Thank you, Senator Warner.

Senator Exon.

Senator **Exon**. Thank you, Mr. Chairman.

Mr. Bowsher, we have done lots of things to try and encourage whistle-blowing in order to crack-down on waste and abuse. How do you think whistle-blowing has generally operated from your perspective and what, if anything, can the Congress do to enhance the whistle-blowing activities which in the end I think probably are our best way at getting at wrongdoing at any level of government and in any one of the services?

Mr. **Bowsher**. I think one thing can be said about the whistle-blowing is that it worked in this case. In other words, people have come forward and raised the issues and told what was happening. I think having the hot lines that we put in in the recent years has been very effective. The number of investigations that are being conducted at any one time, just as you indicate, result—a fair number of times—from whistle blowing.

At the same time, we run one of those hot lines. We have to sort through a lot of calls to get the one call. And so, you can't assume that all of the information that is flowing in through whistle blowing is worthwhile. We spend quite a bit of time and effort running down things that don't really lead to much.

On balance, I think the whistle-blowing laws that are in place now, along with the hot lines and things like that are working fairly well.

Senator **Exon**. Have the whistle blowers been protected as was——

Mr. **Bowsher**. Well, that varies from case to case. I think in some cases they have and in other cases they haven't.

I have always thought that the agencies and the services make a big mistake by getting very harsh on a whistle blower who has done the right thing. And we have had some celebrated cases. I can never understand what the services or the agencies think they are doing when they do that because they generally just create more problems for themselves.

But I think, on balance, that part of the system is working well, as indicated by what has happened here.

Senator **Exon**. From your knowledge of the present investigation that is going on or your knowledge of other matters that your agency has looked into from time to time, are we running into what I fear is another problem where there might not be outright bribery, thievery, waste and fraud but rather failure to deliver as advertised. Maybe it comes under abuse that borders on fraud. It seems to me today that we have increasing numbers of situations where we never get what we pay for. Has there been any indication that this failure to deliver as advertised was covered up so that the end product that we get is not what we purchased?

Mr. **Bowsher**. When we look at the history of these major weapon systems, it is always discouraging that often we get less than what was promised. The only thing we seem to get more of is cost. In other words, the cost generally goes up, the schedule slips, technical milestones slip. And occasionally we get a program in very serious trouble, a shortfall, you might say when compared with what was originally promised. If you go back to the 1960s, you find the same pattern. So, it's a constant problem.

I think one of the biggest issues in this whole procurement area is the issue that Dave Packard always raises, and that involves concurrency versus waiting to get something that you can actually see or kick the tires and make sure it's working before you go into production. Maybe it's because I served under Dave, but I still believe that's the best way of doing it. I think when we have too much concurrency on these weapon systems, we take a big risk. I think that's one of the major issues that has to be decided. In this administration there has been a tendency to allow more concurrency on many of the weapon systems.

Senator EXON. Would you say that maybe that's a line of demarcation or a significant difference from the procurement practices that the United States used in our World War II effort which was a magnificent effort? There was probably some waste, fraud and abuse somewhere along the line even then. But it seems to me, at least looking at it from my perspective, we didn't seem to have all of the difficulties of things not working. After we built the Liberty ship, the Liberty ship worked the way it was supposed to.

Mr. BOWSHER. It worked. That's right.

Senator EXON. Some that can be checked off as more advanced technology, and we press for more maybe.

Mr. BOWSHER. Well, I think that the technology is so different today that we have to recognize this fact. We are in a totally different world technically speaking because electronics today practically drive the success or failure of all these weapon systems, whether we are talking about a ship, an airplane or a missile. In the old days it generally was the motor or it was the fuselage or it was something else that was the key to making the whole thing work. Today if we can't get the electronic systems to work, then we have got a big problem.

Now, I think in time of war, going to concurrency makes a lot of sense. You want to get the best equipment as fast as possible no matter what the cost. But when you are spending as much money as we are spending in peacetime—and we have done it now for so many years—it seems to me we would want a system where we have more successes than what we have had.

We did a study a couple years back, looking at how some of the other countries do their work. I think we looked at West Germany, Israel, France, and the Soviet Union.

Senator EXON. I'm interested in the Soviet Union. We get the impression that they do better at these things than we do. Is that possible?

Mr. BOWSHER. Well, I wouldn't jump to that conclusion——

[Laughter.]

Mr. BOWSHER [continuing]. Because I think they have quite a bit of problems with some of their equipment too. But they do tend to go into production with a more proven vehicle than we do. In other words, they go through a longer R&D effort and have a more extensive prototype phase than we do. In so doing I think they eliminate going into the production phase with something that has to be retrofitted so much when you get it finished. And it is the same with the other countries.

We are the biggest country when it comes to concurrency.

Senator EXON. My time is up. Thank you, Mr. Chairman. Thank you, Mr. Bowsher.

Chairman NUNN. Thank you, Senator Exon.

Senator Cohen.

Senator COHEN. Mr. Bowsher, you indicated that concurrency during peacetime was unworkable, and I agree with that. You said in a time of going to war that we may have to go to concurrency. You don't really mean to suggest that we are living in a time when we can hark back to the days of World War II and perhaps the Korean war and talk about a war scenario in those situations and expanding our industrial production and go to concurrency at that time, do you?

Mr. **Bowsher**. No, no. What I'm just saying is that at that time you would make more changes on the line. You would be heating up the production lines, you would be finding out things from the battlefield that you needed, and you would be putting changes in there on a very quick basis.

But I think that too often our people want to have that kind of an atmosphere in peacetime, and it becomes a very costly way of doing business.

Senator **Cohen**. I tend to agree with your statement about the unenforcement of existing laws. I think whenever we do have laws on the books that go unenforced, it breeds a disrespect and, indeed, perhaps even a contempt for the laws that we already have. But it has been suggested that the existing laws that Congress has been passing may be a causative factor in some of the abuse that has been uncovered. And the question I have regards the Truth in Negotiating Act. Would that be a causative factor in producing these types of scandals?

Mr. **Bowsher**. I don't think so.

Senator **Cohen**. Would the Cost Accounting Standards Board be a causative factor?

Mr. **Bowsher**. No.

Senator **Cohen**. Let me ask you about the debarment rules that have changed in the past 10 years. Senator Levin and I became concerned back in 1979. We found during hearings in the Government Affairs Oversight Committee that there was no policy in the Federal Government for a uniform application of debarment proceedings. We found that one contractor might be convicted of fraud under existing laws, and yet there would be no system for debarring that particular contractor from going across the street and contracting with another agency. Would the debarment provisions that were passed by Congress be one of those types of laws that may have contributed to——

Mr. **Bowsher**. No, I do not think so.

Senator **Cohen**. How about hurry-up spending? You recall that we got very involved in trying to prevent the Department of Defense from unloading a good share of its budget in the final weeks of the final quarter of the fiscal year. That was designed to try and prevent wasteful spending in the last few weeks of the last quarter. Would you call that kind of reform something that contributed to these types of scandals?

Mr. **Bowsher**. No.

Senator **Cohen**. Well, let me finish. How about the Carlucci reforms that the Secretary, at that point a Deputy Secretary, initiated under pressure from Congress because we were going to pass some of those reforms? Were those reforms the type that contributed to this?

Mr. **Bowsher**. Well, I think they might have from one aspect. When you delegate, or devolve responsibility and authority down in a large organization, you need a system telling you what is happening down there. I'm not sure that was put in place, although I'm sure that was what the Congress intended. But I think that's a key element for success any time that you decentralize your management in an organization, especially a large organization.

Senator COHEN. But that doesn't detract from the support that was then offered I think even by GAO that——

Mr. BOWSHER. That's right. In other words——

Senator COHEN [continuing]. Decentralization was not the wrong way to go provided you have the right kind of oversight.

Mr. BOWSHER. That's right. That's right. We supported it.

Senator COHEN. How about competition in contracting? That was something that Senator Levin and myself played a major role.

Mr. BOWSHER. A lot of people are pointing to that, but we do not think that the additional competition is contributing to this.

Senator COHEN. I'm happy to hear you say that too. But there are three or four or five pieces of legislation that Congress has been active over the years in insisting upon, and I would assume you would agree with the statement that it has perhaps been more constructive than destructive in terms of producing the kind of fiscal integrity that we all want to see.

Mr. BOWSHER. Yes.

Senator COHEN. The notion that somehow congressional activity in this area is, in fact, a contributing factor would not seem to be borne out.

Mr. BOWSHER. I don't think the laws that you raised at all have contributed to this.

Senator COHEN. Let me make an observation. The Department of Defense seems to be resistant to almost any congressional initiative, and I say this from experience in a variety of areas. I would point to the chairman and say I recall the reaction of the Department of Defense when we talked about the reorganization of DOD. There was very strong resistance.

I recall also that we were concerned, much as you've indicated, that procurement officers aren't having the kind of incentives to stay in the procurement field and, therefore, get rotated out as quickly as possible, thereby losing expertise in that field.

We found the same thing, for example, on the Joint Staff. We found that we didn't have top people going into the Joint Staff because they saw it as a "dead end" to their career.

Mr. BOWSHER. It has been a problem at the Joint Staff for a long time.

Senator COHEN. Right. So, we have proposed certain reforms in that regard and that was resisted as well. And I could go on to talk about special forces and others. But generally there is an attitude of resistance to "congressional initiatives." And assuming that that resistance is overcome, what you are saying is there is a DOD reactive policy to enforcement. So, on the one hand, you have resistance, and then once you pass the laws, then you have a reactive or sort of benign neglect that is adopted by the Department.

And I'd point to what you said about the internal management control program. Once again, it appears that this is almost a benign neglect of a program that has been put into place to ensure fiscal integrity.

Is that a general problem that we have with any major executive branch or department—the resistance to having these laws "shoved down their throats"?

Mr. BOWSHER. Yes, it does seem to me that over the past 20 years, there is resistance lots of times. I never understand why because I truly think that if the agencies would grab hold of some of those things and really implement them well, then it would be extremely beneficial. I think the Financial Management Integrity Act is a good example. That was passed, again coming out of the Government Operations Committee. What that says is once a year the management of each agency has to assess its internal controls, and tell what weaknesses they have and what it plans to do to correct them. You should use your internal audit or your IG function to go out and review the progress being made. The implementation of this act has been turned into a paperwork exercise by so many of the agencies that it is pathetic.

Senator COHEN. One more question if I might, Mr. Chairman.

What are the penalties for this sort of treatment of the act itself? What are the penalties for noncompliance as such or the benign neglect attitude that has been evidenced by the agencies? Is it simply a political repercussion that we are seeing now?

Mr. BOWSHER. That's all. In other words, you might have another congressional hearing down the road that you would just as soon not have, but that's about all. I think Congress has just got to get tough on the issue of getting good information from these agencies, financial information, where are the controls, where are the systems; in other words, get on top of your operation.

Senator COHEN. And one final point, if I might.

You indicated in your opening statement—I think it's on the first page—that the military now has a problem of too many systems chasing too few dollars. You're not implying, are you, that if you had fewer systems chasing fewer dollars, you would avoid the problems that we currently have.

Mr. BOWSHER. No. What I'm implying there is that in their FYDP, in their PPBS system, they have too many programs. That system, which was designed back in the early 1960s, was intended to give good visibility over what programs were going to be approved to avoid having more programs than you could afford. The unfortunate thing is that they have crammed so much into that system, and generally with low cost estimates, that you've got more program than what you can afford.

Senator COHEN. But you might want to have fewer systems with more dollars in order to avoid the kind of stretch-outs of production rates that you're not achieving. So, it's not just a simple formula of fewer systems and fewer dollars. You've got to have the management oversight, but you also might want to have fewer systems and more dollars.

Mr. BOWSHER. That's correct.

Senator COHEN. Thank you, Mr. Chairman.

Chairman NUNN. Thank you, Senator Cohen.

Senator Levin.

Senator LEVIN. Thank you, Mr. Chairman.

Mr. Bowsher, I want to talk to you about consultants first. There are two types of consultants: one, the consultants to the companies, and the other kind of consultants are the consultants that we hire directly by contract, that the Government hires directly.

The investigation has tended to focus on consultants to companies and how they were able to obtain access to information they shouldn't have access to and then shared it with their clients. There has been a great focus on that, properly so. It's the improper acquisition of inside information and sharing it with your client.

What I want to ask you about is a much larger group of consultants perhaps, although we don't know the exact numbers, which are the ones that we hire to give us advice. In many cases those consultants not only have us as clients, but they have their own private clients.

Mr. BOWSHER. That's correct.

Senator LEVIN. And unless they are special employees of the Government or serve on Federal advisory committees that are properly chartered—which is a very small number of consultants—those contract consultants of ours are not governed by any disclosure laws as far as I can see. Do you agree with that?

Mr. BOWSHER. I believe that's right, Senator.

Senator LEVIN. I am very much troubled by that because we have a situation then where there is no requirement that somebody who gives us advice is required to disclose who else he or she is giving advice to. That seems to me to be ripe for both conflicts of interest and appearances of conflict of interest. I am wondering if so far you would agree with me.

Mr. BOWSHER. I agree with that.

Senator LEVIN. Because I'm going to be proposing to the Secretary of Defense—we are working on a proposal to include consultants in disclosure requirements, just the way special employees have to disclose. And I would hope that you might be able to give us some support in that area.

Mr. BOWSHER. Yes. I would like to do some checking, but on balance I think I would support that proposal. As we do our review on the consultant area, we will look at all of this.

Senator LEVIN. What's ironic is that we spent a lot of energy—and very properly so—on people who improperly have access to information, who aren't supposed to have access, how they do it and what they do with it. And it's important that we do foucs on that in any prosecutions and investigations.

But you've got this huge number of people who are properly in possession of information. Indeed, they may have helped create it. They're consulting with us. We're paying them. They're not bribing us to get it. We're paying them to give it.

Mr. BOWSHER. I think this also shows the change that has happened, going back to Senator Exon's question, that today these weapons are so technical in nature that frequently you have to reach out and get advice. So, what you're saying is we had better find out what are the relationships of these people who are giving us advice.

Senator LEVIN. Absolutely. There are going to be times that we're going to want to get advice from somebody who is also giving advice to a private client. We know that. But we surely ought to be in a position where we can assess it before paying for that advice.

And I will be sending you that proposal so perhaps you can help critique it before we——

Mr. **Bowsher**. We'd be pleased to do that.

Senator **Levin**. DOD can do without new laws, by the way. We shouldn't have to require DOD to require their consultants to disclose their private clients. That's something that DOD ought to be willing to do, I hope, on its own.

Do you know what the Department of Energy rules are on disclosure of private clients by consultants? I understand they are much more extensive than the DOD rules. Do you happen to know?

Mr. **Bowsher**. I think we had better provide that for the record.

[The information follows:]

The Department of Energy's regulation concerning special government employees' (consultants') disclosure of private clients is contained in the Code of Federal Regulations at 10 CFR 1010. According to that regulation, special government employees are required to file a disclosure form listing their financial affiliations. In addition, special government employees paid at a rate equal to or greater than the minimum rate for a GS-16 on the general schedule are required to file a form identifying any entity that paid them $2,500 or more in any of the 5 calendar years prior to their appointment. Special government employees hired by DOD file a financial disclosure form but are not required to disclose prior employers.

Senator **Levin**. You've made reference to—I believe you've made reference to—the relationship between the Department of Defense and the Department of Justice in the investigation and the prosecution of these cases. You indicated in your oral testimony that if there's an indication that someone is going to be indicted, that then perhaps that person should be suspended or in some way——

Mr. **Bowsher**. No, if a person is indicted, that constitutes adequate evidence for suspension.

Senator **Levin**. All right. What happens in the current situation where the Justice Department is in possession of information that they believe is highly suspicious but it has not yet led to an indictment; indeed, it hasn't even gone to a grand jury? What should be the role of the Justice Department in alerting the Department of Defense to that, and is there anything the Department of Defense could do even if they knew about that?

Let's assume there is evidence. It has not yet led to an indictment, indeed, maybe never will. We don't know for sure that it will. But there's a great deal of evidence that has come to the Department of Justice's attention. They believe there's reasonable prospect. They'll ask a grand jury for an indictment, but it may take 60 days. The Department of Defense is now in the process of negotiating contracts in an area, including with that contractor. Should they hold off on that kind of a contract or not?

Mr. **Bowsher**. Well, I'm sure the Justice Department people and the investigative people would say yes.

Senator **Levin**. Can they properly even share that information with the Department of Defense?

Mr. **Bowsher**. Jim Hinchman, my attorney, has pointed out that he thinks they can share such information with the Department of Defense. The Department of Defense cannot, though, divulge that in any public arena or probably take any official action. It might guide them, though, in how to proceed.

Senator **Levin**. Can they delay entering into a contract based on that information?

Mr. **Bowsher**. Oh, sure.

Senator **Levin**. My time is up. Thank you, Mr. Chairman.

Chairman **Nunn**. Thank you, Senator Levin.

Senator Quayle.

Senator **Quayle**. Thank you, Mr. Chairman.

Mr. Bowsher, I want you to, if you could, identify for us from your viewpoint the three most significant areas of the procurement process that are vulnerable or weak to the type of allegations that we have read about. Can you get to three areas that you really think the system is weak and would perhaps induce or allow this kind of behavior or culture to develop over the months?

Mr. **Bowsher**. The first area would be specifications. In other words, just as we were saying a minute ago with Senator Levin, there's a lot of reaching out to get advice when writing specifications, when doing concept design and things like that on these weapon systems. At that point, you ought to have a system that is pretty vigilant so that you get the advice that you need, but it can't be used later on or shouldn't be used to give one contractor an advantage over another.

Senator **Quayle**. Certainly we don't want to give one contractor advantage over another. But as we look to the specifications to make sure that we come up with the best specifications and the best quality, we want to be able to have some free flow of ideas——

Mr. **Bowsher**. Yes, that's right.

Senator **Quayle** [continuing]. And discussion of the technical data.

Mr. **Bowsher**. Yes.

Senator **Quayle**. And what I'm trying to pinpoint from your viewpoint are weaknesses or vulnerabilities that you see in the system right now. I mean, trading information back and forth, yes. What allows this trading of information? Is there something that really allows this trading of information? Is the Government getting it and trading it to various contractors, or is that prohibited as the system stands now?

Mr. **Bowsher**. I think the laws and regulations quite clearly prohibit it. So it's a case in the management of your organization. I'm talking about two sets of management now when I talk about management.

Senator **Quayle**. The management of the system.

Mr. **Bowsher**. Yes. In other words, you have got management at the Department of Defense and then the services. And then you have got management of these companies. The management of these companies—the top management, the audit committees, the directors of those committees. They have got to make a major effort to make sure that they don't have employees or consultants who are taking advantage of this system.

Senator **Quayle**. You are talking about defense contractors now.

Mr. **Bowsher**. I'm talking about defense contractors. In other words, you have to have the management of industry involved, much as we did in the early 1970s when we ran into sensitive payment problems, if you remember—bribes overseas. A lot of people said we would never get on top of that, but actually we enacted some legislation and we put the onus, on the leadership of our corporations not to be condoning that kind of behavior.

I think that's one of the things that ought to be looked at now in this defense arena because I don't see the leadership of the defense industry willing to do it just on a voluntary basis. In other words, they have to say to their people we don't want any bribes given and we don't want any consultants out there giving you information they shouldn't give you. You have to put a lot of emphasis on the companies to have integrity in their operations.

Then you move over to the Department of Defense, and you have to do the same with Defense management. You have to make sure that as they bring people aboard to give them advice from the private sector, you know what their relationships are. You have got to make sure that those people aren't going to abuse those relationships.

You can't pass a law to handle everything. Lots of times it will depend on the integrity of your management. This is a tough area because you're dealing with a big government organization and a big private sector group of contractors. Some of the recent initiatives of the SEC ought to be looked at by this committee and the DOD management team—I've already talked to Secretary Carlucci about this—to see if there are some ways to get tougher through the management of the defense contractors.

Senator **QUAYLE**. So, as you look at this defense procurement system in its entirety and try to zero in on a weakness or vulnerability, you would look to the defense contractors. And if I hear you right, you are talking about some code of ethics.

Mr. **BOWSHER**. A code of ethics along with an annual review—an annual review that is included in the annual report and reviewed by the audit committee of the board of directors.

Senator **QUAYLE**. Now, this would be a voluntary code of ethics or would you legislate——

Mr. **BOWSHER**. No, no. I would——

Senator **QUAYLE**. Make it a voluntary code of ethics.

Mr. **BOWSHER**. But maybe reviewed by people at Defense.

Senator **QUAYLE**. Reviewed possibly by the people at Defense. And then you say on the Defense side, that you have to make certain that the people that you hire don't have any potential conflicts——

Mr. **BOWSHER**. That's right.

Senator **QUAYLE**. Are honest——

Mr. **BOWSHER**. That's right. And you also need a final independent review as I was discussing with Senator Warner just a while back. We used to have that at the Navy in the Navy Materiel Command. In other words, no matter what the Air Systems Command had done as far as concept formulation for an airplane or something like that, when they finally got ready to write a contract, it had to go through an independent group at the Navy Materiel Command. Those are some of the controls you have to have in your organization.

Senator **QUAYLE**. Well, you have the final selection authority.

Mr. **BOWSHER**. Yes.

Senator **QUAYLE**. Well, I mean, you have three or four layers right now of review on the source selection process. You are saying another one on top of that?

Mr. **Bowsher**. I'm saying an independent one off on the side. In other words, it's the same way as we review our GAO reports. I look at the line organization. I have layers of management above the team that is preparing that report, but I also send it through an independent group that has never worked on the report to make sure that they see the evidence that supports the recommendations. Those are the kind of features you have to build into this procurement process.

Senator **Quayle**. My time is up. I just want to make sure, Mr. Chairman, that I understand this.

Looking at the problems that we have, we basically have the three areas that you have identified. It's one on the management side, some sort of voluntary code of ethics and reviewed. On the Government side, you better make sure you hire good people, which to me is sort of a management issue. And finally, you think that there ought to be some sort of a final independent review that from your viewpoint these are the vulnerabilities as you see it in the procurement process.

Mr. **Bowsher**. Yes.

Senator **Quayle**. Thank you.

Chairman **Nunn**. Thank you, Senator Quayle.

Senator Bingaman.

Senator **Bingaman**. Thank you, Mr. Chairman. I do have a statement I'd like to put in the record, if I could.

[The prepared statement of Senator Bingaman follows:]

PREPARED STATEMENT BY SENATOR JEFF BINGAMAN

Mr. Chairman, I want to echo your welcome to Mr. Bowsher and your emphasis on the need for these hearings not to interfere with or in any way compromise the on-going investigation into defense procurement fraud. As a former state Attorney General, I know how important it is to allow the investigation of complex fraud cases to proceed in confidence.

The Defense Industry and Technology Subcommittee has had representatives from both the General Accounting Office and the Defense Department's Office of the Inspector General testify before it the past two years and we have benefited greatly from that testimony, as I am sure we will again today. I have found their expertise essential to understanding the problems facing the current acquisition system.

Let me also add that those hearings in the Defense Industry and Technology Subcommittee have produced convincing evidence that we have fundamental problems in our defense acquisition system, problems which are deeply embedded in the current system and which a quarter century of reform efforts have not resolved. Indeed, one of the fundamental problems is the complexity of the process built up by the series of well-intended reform efforts.

But in addition to the problem of complexity, we have serious problems recruiting and retaining the sort of people we need in our career acquisition workforce. Many studies, most notably the Packard Commission, have pointed to this as a critical problem which urgently needs to be addressed. We do have legislation before the Senate right now, S. 2530, which would allow the next Secretary of Defense to design a more flexible and responsive personnel system for up to 100,000 DOD civilian acquisition personnel. I hope the Congress will pass that legislation this year.

We have many other fundamental problems in our acquisition system as well. The Chairman has discussed the mismatch between the acquisition system and the budget process. The Defense Department starts far more programs in the acquisition system than likely future budgets will sustain. That guarantees waste in the form of inefficient production rates and stretching out of programs.

Our subcommittee hearings have also told us that we have today an acquisition system that takes ever longer to develop and field weapons, that works against innovation, that puts inadequate emphasis on controlling costs and on quality, and that is suffering from regulatory and legislative overload.

To that list, we are clearly going to add additional problems as we monitor the current fraud investigation and as we probe in these hearings into such issues as the role of consultants, the protection of proprietary information in the source selection process, conflict of interest rules, and the adequacy of the resources available to our fraud investigators and prosecutors.

It is going to take time to get to the heart of these issues. There are likely to be no quick-fixes or easy answers. History tells us that we should approach the problems of the defense acquisition system with a great deal of humility. Many of the problems Secretary McNamara and other reformers identified more than two decades ago are still with us, and the list of problems has lengthened as the complexity of the system had increased since then. Sustained management attention by both the Secretary of Defense and the Congress over a period of years is going to be needed to insure we get a dollar of defense for every dollar we put into the defense acquisition system.

Senator BINGAMAN. Mr. Bowsher, let me ask a couple of questions following up Senator Quayle's comments. You talk about an independent group that has not been involved that makes decisions before the final report goes out in your organization. Are you suggesting that an independent group should be in place to review decisions on who gets contracts before contracts are let?

Mr. BOWSHER. No. More to review the process, to review who was involved, and whether all the rules and regulations have been followed. The source selection authority and the advisory board process is quite adequate to make the best judgment.

Senator BINGAMAN. Let me ask on existing——

Mr. BOWSHER. Let me give you an illustration, if I may, because I think it might help.

Senator BINGAMAN. Go ahead.

Mr. BOWSHER. If you are going to build a new ship or a new aircraft you might want to use a certain type of contract, such as a cost plus incentive that gives you more flexibility in building the first one. Other people would say, no, let's use a fixed price contract. It seems to me that instead of having a situation where everybody drives their own thing, you would be better off with an independent group that would make sure you have followed the rules and regulations.

Senator BINGAMAN. Now, on the contracts that are allegedly involved in the present scandal, my information just from reading the newspapers is that what's involved here essentially—or at least a lot of what's involved here—is people getting access to proprietary information and by doing so, particular contractors got an advantage in the competition and bid the thing lower or bid with more specificity or some way or other improved their bid so that they got the contract. Is that your understanding?

Mr. BOWSHER. That's my understanding too. That's right.

Senator BINGAMAN. Under that scenario, does DOD have authority to cancel contracts that are obtained by that kind of illegal method?

Mr. BOWSHER. Yes, DOD has authority to rescind contracts where there has been a final conviction for bribery or similar misconduct; also if you have an indictment, you can suspend the contractor; if you have a conviction, you can debar a contractor. So, if any of these people go to trial and if the corporation or any of their senior officials are convicted, then they could be debarred.

Now, as far as termination of the contract, that's easy enough if it's a small contractor because you can get somebody else to do it.

Where you run into problems is when you are dealing with the big prime contractors because you need the submarine or you need the plane, and other contractors are not readily available. So it's not so easy to terminate big prime contractors—and that's been one of the great dilemmas in defense procurement. The Government is dependent on a relatively few big prime contractors.

Senator **Bingaman**. Even without indictment and even without conviction, though, if the Department of Defense is satisfied that a contract was obtained because someone illegally obtained inside information, you are saying they do not have the authority to cancel that contract unless they get an indictment.

Mr. **Bowsher**. Yes. They could only do it on the basis of what's known as termination for convenience. And then, of course, the Government has to pay for pretty much whatever has been done up to that point.

Senator **Bingaman**. I see. Other than that, they have to get an indictment.

Now, why don't they have a provision in those contracts that gives them that authority absent indictment? I mean, that is strictly a matter of contractual law between the contractor and the Government. Is there any reason why they don't have that written into the contracts?

Mr. **Conahan**. Termination for cause.

Mr. **Bowsher**. That's right.

Mr. **Conahan**. Well, the cause in this case would be because they obtained improper data or shared improper data. Now, that is the management. That's the administration's way of handling that. Now, out here, there is also possibly a legal avenue to be pursued.

Senator **Bingaman**. But you are saying that if the Department of Defense determines that someone has obtained illegal information or information that they did not legally have a right to have, they have the ability to cancel that contract regardless of whether the Justice Department ever does anything.

Mr. **Bowsher**. Yes. But then they have to prove it.

Senator **Bingaman**. They only have to prove it if the contractor takes them to court.

Mr. **Bowsher**. In other words, if the contractor offered a gratuity to a government employee in order to obtain a contract, the Government may terminate the contract under the gratuities clause, but only after notice and a hearing. You have to prove your case. So, the first part of my answer wasn't quite right there, Senator.

Senator **Bingaman**. Your comments about the Justice Department concern me a little bit. I gather that you have real questions as to whether the Justice Department is presently equipped and staffed and otherwise has the resources to do what they have taken on to do in dealing with this series of cases. Are there things you think we should do in the Congress this year to ensure that the Justice Department has the resources and has the internal management functions going that ensure that these cases are properly prosecuted?

Mr. **Bowsher**. Well, the Justice Department needs a little better organization with respect to the flow of information on the cases. Now, they claim, in reply to our report, that they don't take issue with some of the problems and concerns we raised. But they also claim that the budget was cut. In tracing it back, we did note that there were some reductions in the budgets, and we are still trying to trace the sequence of events in these budget cuts. We will have that by next week, so we can provide it later. I can provide the report, and I can provide the history on the budget cuts next week.

Senator **Bingaman**. Will you also be able to give us any recommendations on additional budget needed?

Mr. **Bowsher**. Sure.

[The information follows:]

As indicated in our report (GAO/GGD-88-96), the Department of Justice does not know how many attorneys are being used for defense procurement fraud investigations and prosecutions. GAO found that the Department of Justice needs more and better information to decide how many additional attorneys it needs. Without this kind of information, it is difficult to say what additional funds are needed. If the Justice Department needs more attorneys, it should be able to tell the Congress: (1) how many attorneys are being used in this area and what it is doing with these resources and (2) exactly how it plans to use the additional attorneys.

Regarding the budgetary information we promised to provide, we obtained the following information relating to Justice's "General Legal Activities" and "U.S. Attorneys (Criminal)" budget categories. General Legal Activities covers, among other things, headquarters criminal; claims, customs and general civil; land, natural resources, and Indian; and civil rights matters. U.S. Attorneys (Criminal) covers criminal-related work by the U.S. Attorney's Offices.

DEPARTMENT OF JUSTICE COMPARISON OF BUDGET REQUEST TO CONGRESSIONAL APPROPRIATION

[General legal activities, in thousands of dollars]

	Budget request	Appropriation	Dollar difference	Percent difference
Fiscal year:				
1980	$109,142	$112,620	$3,478	3.2
1981	123,750	120,950	(2,800)	−2.3
1982	126,713	130,405	3,692	2.9
1983	148,787	145,428	(3,359)	−2.3
1984	180,701	169,637	(11,064)	−6.1
1985	207,906	197,575	(10,331)	−5.0
1986	207,283	180,714	(26,569)	−12.8
1987	232,783	220,856	(11,927)	−5.1
1988[1]	303,485	238,209	(65,276)	−21.5
Total	1,640,550	1,516,394	(124,156)	−7.6

[1] Does not include supplemental appropriations.

[U.S. attorneys (Criminal), in thousands of dollars]

	Budget request	Appropriation	Dollar difference	Percent difference
Fiscal year:				
1980	$88,868	$86,904	($1,964)	−2.2
1981	96,360	99,015	2,655	2.8
1982	96,731	107,665	10,934	11.3
1983	118,195	121,755	3,560	3.0
1984	134,600	134,760	160	0.1
1985	153,445	155,145	1,700	1.1
1986	194,204	165,158	(29,046)	−15.0
1987	197,367	195,952	(1,415)	−0.7
1988[1]	233,728	209,366	(24,362)	−10.4
Total	1,313,498	1,275,720	(37,778)	−2.9

[1] Does not include supplemental appropriations.

Senator **Bingaman**. Thank you very much, Mr. Chairman.

Senator **Exon** [presiding]. Thank you, Senator Bingaman. Senator McCain.

Senator **McCain**. Thank you, Mr. Chairman.

Thank you, Mr. Bowsher, for your very important testimony here today. I think it is very credible and very important in helping us address this terrible problem.

The first question I would like to ask—it has probably already been asked—is in your view from the information you have, how widespread is this scandal? I have heard that it is far worse than anyone ever imagined. Some say that it is only a few individuals and maybe some companies. The reality is that there are thousands of companies and corporations that do business with the Defense Department. Could you, to the best of your knowledge, give us some idea as to the extent and scope of this problem?

Mr. **Bowsher**. We don't have any more information than what we read in the papers. Earlier, somebody asked me to differentiate between this scandal and the previous scandals—and I said—to me the most significant thing was this seems to be higher up. In other words, in the private sector we often differentiate between management fraud and ordinary fraud. And at the Assistant Secretary level, if it's to be proven at that level, and the Deputy Assistant Secretary level seems to me to be very close to what I would call a significant management fraud.

Now, how many people are involved—it might be a few people that networked out, you might say, and maybe it isn't as widespread as it appears at first. But how totally widespread it is, we don't have any information other than what we are reading about.

Senator **McCain**. Would you hold the same view as far as how "high up" in the companies that are doing the business?

Mr. **Bowsher**. Yes, I would. In other words based on what I've read so far, when you reach the vice president level in defense contractors, you are reaching senior management. That's one of the things I was discussing with Senator Quayle. I think that Congress and the Defense Department ought to look very hard at instilling a little more discipline into the process. A little more responsibility should be given to senior corporate officials, boards of directors and audit committees to make sure that it doesn't happen.

Senator **McCain**. Do you view this as a lot of corporations involved, or do you have any feel for that?

Mr. **Bowsher**. I only know what I've read in the papers as far as the number of corporations.

Senator **McCain**. I'd like to talk to you for a minute about this business of competition. All of us want everybody to compete for the lowest possible price and get the best bang for our buck, as we always say. Yet we seemed to be plagued, as you were mentioning a little while ago, with this business of only a very few "prime" contractors. How do you get around the problem that if, suppose, we are bidding for a new aircraft and Boeing Aircraft has built the last two new aircraft and they come in with the lowest bid on the next one? How do we resolve that to the American people. How do we explain the requirement that we have to keep a certain number of people in business and at the same time come up with the best product at the lowest cost?

Mr. Bowsher. I think it's just one of the tough features of defense contracting and running the Defense Department. I am a great believer in competition, but there's no question that one of the things you have to consider from time to time is your defense mobilization base needs and how many contractors you have to keep. I was asked earlier did I think competition has contributed to this scandal. We don't see any evidence of that yet. It might be one of the driving forces, but even when you have sole source, the tough thing in this business is getting that major contract. That's what everybody goes after, and whether or not it's under a more competitive basis, I think there's a lot of pressure. I don't underestimate that for a moment.

Senator McCain. When a contract is awarded wouldn't it be better for the taxpayers to know that that contract was awarded because of our protection of the defense mobilization base rather than telling them that they've got the best contract? Clearly sometimes perpetuation was a factor?

Mr. Bowsher. Yes. I would see nothing wrong with making that known.

Senator Cohen. Would you yield.

Senator McCain. Sure.

Senator Cohen. Aren't they required to do that now? You have contractors competing and you have a lower bid, and yet the contract is awarded to another contractor. That is disclosed publicly now.

Mr. Bowsher. Yes. I think it is. We were just checking with our experts. Under the CICA laws, if the contract is awarded to someone other than the lowest bidder it has to be spelled out and announced.

Senator McCain. Let's talk about program managers for a minute. I think there is a widespread belief that the career of the program manager rises or fails with the success or failure of his program. Part of the criteria for the success or failure of his program rests on the costs of the particular item that he has supervision over. How do you get around this recurring and continual problem of years with scandals or without scandals when you are presented knowingly with an unrealistic initial cost? Even if it's a "fixed-price" contract—we have seen that. And over time we see the cost of the program escalate dramatically. The program manager changes. Corporate memory fades and we end up with another scandal on our hands.

Mr. Bowsher. It's a terrible part of the procurement process. We often have too many program managers in the life of a weapons system. And often, I have always felt that the bad news is programmed to come out later from a budget strategy point of view, and sometimes from a career point of view. You just never know what is the motivating factor. But people don't disclose cost overruns when they first learn about them. There's a lot of strategizing on when to notify the senior people at Defense and also the Congress when there's bad news.

Senator McCain. Even though I believe there are laws on the books requiring notification as well.

Mr. Bowsher. Exactly, yes.

I think that this is a problem that has plagued the process for a long time. I think the only way you ever get a handle on it—and I saw it only happen once or twice over there—is when you get somebody at the top says I want to know all the bad news now; I want to get it out on the table. I saw Laird do it when he first became Secretary of Defense. One of the reasons he did it, though, was the C-5 cost scandal was thrown out on the table just as he arrived. So, he wanted to find out how many more of those were in the building. As a result, I would say that at that time we really knew what our problems were because we announced that we had $16 billion worth of cost overruns. But from that point on, we went back to the same old game of let's be careful when we notify others.

Senator McCAIN. My time has expired so I won't ask you about how we get around the problem of planes, trucks and ASW equipment at the dictates of Congress, when all objective evidence indicates that we shouldn't. But I don't have time to ask that. [Laughter.]

Chairman NUNN [presiding]. It sounds like that was the answer. What was the question? [Laughter.]

Senator McCain, go ahead if you'd like.

Senator McCAIN. Thank you, Mr. Chairman.

Chairman NUNN. Let's see. Next on the list is Mr. Dixon.

Senator DIXON. Mr. Chairman, first of all, I ask that my statement regarding this subject matter be put in the record.

Chairman NUNN. Without objection.

[The prepared statement of Senator Dixon follows:]

PREPARED STATEMENT BY SENATOR ALAN J. DIXON

Mr. Chairman, we are pleased to have the Hon. Charles Bowsher, Comptroller General of the United States, with us today as we begin our review of the defense acquisition process.

Just last Friday I introduced Senate bill S. 2621, the Department of Defense Procurement Improvements Act of 1988. This legislation establishes the Under Secretary of Defense for Acquisition as a true acquisition and procurement czar within the Department of Defense. The legislation centralizes authority and responsibility for acquisition policy in a single office. It also establishes parameters for contractors, consultants and Government officials involved in Government contracting.

As the chairman knows, I also introduced the legislation that initially created the Office of the Under Secretary of Defense for Acquisition. At that time I had to engage in battles with the Secretary of Defense and the service Secretaries. The original bill gave the Under Secretary complete responsibility for supervising the entire defense acquisition system but the Pentagon resisted this essential reform and a weaker version of my legislation became law.

Mr. Chairman, we cannot totally legislate away greed and corruption but we must do everything possible to correct the inherent inefficencies of the current system and reduce the potential for abuse. The cause of national security should not be a shield for incompetence, mismanagement, corruption, and cronyism.

I look forward to hearing Mr. Bowsher's views on the defense acquisition system. Thank you.

Senator DIXON. Mr. Bowsher, I thank you very much for your testimony which I think has been very helpful to the committee.

I want to go along on two lines of questioning here. First, in a general sense about the procurement and acquisition policy of the Department of Defense. I want to talk about that a little bit. And then interestingly, because you mentioned the DIVAD gun in your testimony and I had an experience with that, I want to pursue that as an example of one of the things that concerns me.

When the distinguished chairman and the then chairman, Senator Goldwater, worked on the DOD Reorganization bill and we were here involved in that, it was quite apparent to us that the services were not happy at all with this idea. And you mentioned Dave Packard who I think made a major contribution at that time, as you know.

Mr. **Bowsher**. That's right.

Senator **Dixon**. I recall his testimony. And I was active, as you know, in passing the legislation for the Under Secretary of Defense for Acquisition. There was tremendous opposition to that and the services, particularly from the Navy, may I say, which seemed to have the bulk of the trouble right now in what we read in the newspapers.

And then Mr. Godwin was appointed the Under Secretary for Defense for Acquisition. And all he had was problems. He finally threw up his hands in disgust. He resigned. We had hearings here and he sat in that chair and expressed to us his concerns because there was no cooperation in the various services. And I think that continues to be true. I think Dr. Costello is probably able to work within the system a little better and is having some success.

But wouldn't you say that it is a fact that the tremendous consciousness of their own interests in the respective services leads to some problems in acquisition and procurement in the system?

Mr. **Bowsher**. Yes, it does.

I think the very unfortunate situation with the Godwin incident was that you had somebody with a lot of background who was brought into the job and he knew what he had to do. He came over and had lunch with us at GAO, and he spelled out what he was going to try to accomplish. One of the things he was going to try to accomplish was to learn where things stood. He ran up against all kinds of opposition trying to find out where these programs stand. And if you're not going to have that information available, then you set up an environment, an atmosphere in which people keep secrets down in the organization. And that is one of the great things that leads to these kinds of problems.

Senator **Dixon**. Let me pursue that because the DIVAD is a good example. I was sitting over there where my friend from Arizona is now sitting, and his colleague, Senator Goldwater, was chairman the day we brought up the question of the DIVAD gun, and I suggested it might not be too good. And the senior Senator from Arizona at that time, the chairman of the committee, authorized me to go down there and have a look at it. And I went down to El Paso and I went out there and tested the DIVAD gun.

Chairman **Nunn**. What he said was that it's so good that even you can handle it.

Senator **Dixon**. That's right. [Laughter.]

He said it's an idiot gun. Even you can hit something with it. That's exactly what he said.

I went down to Fort Bliss, and what came through immediately was here's this group of people down here. This is an Army acquisition, and they are interested in making this a great success. They already have 55 of those things, great big tanks with two Bofors cannons on them and an F-16 radar set all married together in a marriage that didn't work. The left gun quit firing after 7 attempts, and in 88 attempts we didn't hit anything.

But the point is they had already bought and had in place 55 of those great big monstrosities, which I guess they've still got somewhere. And this was their acquisition, don't you see? And I'll never forget at the end of the day going back in the vehicle with the commanding general in charge of that acquisition of the DIVAD gun who said, Senator, I feel so bad. My baby failed today, didn't it? His baby, don't you see? The acquisition policies of the separate services competing to get their share and do things not in the whole interest of the country it seems to me so many times, but just in the advancement of their own acquisition policies in their own branch of the service.

Now, isn't that something that good people like you that have the expertise could try to look at and try to define for us a way in which we can respond to that and give a sense of wholeness to this whole acquisition and procurement policy?

Mr. **Bowsher**. You know, that's really why you set up the Office of the Secretary of Defense. If you go back, Harry Truman didn't want to have to make these type of decisions any longer. That is, what Air Force wanted versus the Navy and the Army. And so, it has always been disappointing to me when we go through periods of time when the Office of the Secretary of Defense does not create an atmosphere in which they are willing to look at everybody's weapon. We are willing to support a certain number of them, but we can't support them all. And then what we want to do is find out which ones work.

In industry you develop products that don't work, and you cut them off. That is one of the things that we do so poorly in the Defense Department and in government in general. We are not willing to say, you know, it was a good idea, but it isn't working. Let's quit and come up with another idea. And that's really one of the major functions of the Office of the Secretary of Defense to have a good testing program, to know what is working, what isn't, and to make the tough weapons system decisions.

Senator **Dixon**. What in your opinion could be done to have more direct line authority in the Under Secretary of Defense for Acquisition acting, of course, in the place of the Secretary of Defense into the various services to have control and direct line authority over this whole process? And I don't mean buying rulers and pencils and pens. I'm talking about all stages of the various weapons systems, particularly the major weapons systems and things like that. How can we somehow dominate the buddy system that still exists so profoundly and make it work in a better way in your view?

Mr. **Bowsher**. I think two or three things can be done. You have to, one, get four very capable people: the person at the Defense level and the three service Secretaries so that you have a civilian team that is knowledgeable, willing to work together and to make the tough decisions. Then you have to get an information system, just as Mr. Godwin was trying to do, to know where things stand. Then you have to energize your staff to go out there to do just what you did, go out into the field and see how it's working. Those four people, the Under Secretary for Acquisition at the Defense level and the three at the service level—if they were supported by the Secretary of Defense, could do the job.

Senator DIXON. My time is up, Mr. Chairman, I thank the Chair.

Chairman NUNN. Thank you, Senator Dixon.

It's apparent that Mr. Godwin did not get supported at the Secretary of Defense level.

Mr. BOWSHER. That's correct.

Senator DIXON. He could not get the basic information he needed.

Mr. BOWSHER. That's very obvious.

Senator DIXON. Do we think that has improved any, Mr. Chairman, now? We don't hear squawks anymore.

Chairman NUNN. That's a good question for the witness.

Mr. BOWSHER. We do not have any impression that there has been a major improvement. I think they will state they are working on it. We are going to include that as part of our review so that by next January or February, we will be able to tell you officially what we think.

Senator DIXON. I think that would be valuable, Mr. Chairman.

Chairman NUNN. I'd say even before that. It seems to me that right at the very beginning of a new administration, whether it's a Republican or Democratic President, you have to have a sense of what kind of team you're getting together at the Department of Defense. If the President selects a Secretary of Defense and the Secretary of Defense then has to struggle to put his team together, and the White House is involved in every single decision, and you get basic key people appointed based on how much activity they involve themselves in in a political campaign without the requirements of being a part of a team that has got a lot of management expertise, then you've got a disaster to begin with.

Do you have any recommendations to make along that line?

Mr. BOWSHER. Yes, I'd like to second that very much, Mr. Chairman. I was there when the Secretary of Defense had practically total say over who was on his team. He had to clear it with the White House, but I served under McNamara, Clifford and Laird, and they had strong teams. They had strong civilian teams, knowledgeable people. And you are talking about your 30 top Presidential appointees at the Department of Defense. The White House personnel office couldn't give them an unqualified person, and, therefore, you had real leadership in some of these areas at that time.

Chairman NUNN. The same thing would apply to the service Secretaries. Right?

Mr. BOWSHER. Absolutely.

Chairman NUNN. You would have to have service Secretaries that basically respond to the Secretary of Defense.

Mr. BOWSHER. That's right. You cannot have everybody going off with their own agenda. And that was part of this problem I think.

Senator DIXON. If I could just make this comment, Mr. Chairman. I can't think of a weirder experience than going to breakfast with the Under Secretary of Defense for Acquisition, Mr. Godwin, after we had passed the legislation, the Packard Commission report. The Congress passed the legislation.

Chairman NUNN. And the President endorsed it.

Senator DIXON. And I think my friend from New Mexico was at that breakfast—I believe he was, Mr. Levin and some others—when the fellow just said, well, I don't know. I can't get anything done around here. Nobody will cooperate with me. We just can't get this thing to work. We can't function. And it was a kind of a weird sensation to know that here we had the President for it, the Packard Commission for it, the Congress for it, but the service Secretaries weren't going to let it happen. That was all there was to it.

Chairman NUNN. Well, at that stage the Secretary of Defense had to step forward and go to bat, and he didn't do it.

Senator DIXON. That's true, of course.

Chairman NUNN. Senator Cohen.

Senator COHEN. I have one question for Senator Dixon. I wondered did Senator Dixon tell that general that his baby appeared to be born out of wedlock? [Laughter.]

Or just out of a bad marriage?

Senator DIXON. It was sure a bad marriage.

Senator COHEN. Well, just to pick up on what Senator Dixon was saying about the lack of enthusiasm for the reforms that are, in fact, passed, you may recall that about nearly 2 years ago now—1½ years ago—we passed the program Fraud Civil Remedies Act. Are you familiar with that act, Mr. Bowsher, in which regulations were supposed to have been issued by April 1987. We have GSA, NSA, almost every other major agency has now issued regulations. The DOD IG testified that this law was the single most important piece of legislation to combat fraud since the False Claims Act. Still, DOD has yet to issue any regulations pursuant to that act. One more indication.

Mr. BOWSHER. I think it's just one more indication. That's exactly right.

Senator COHEN. One final point. You have had some discussions with Secretary Carlucci. Have you reviewed with him some of the deficiencies you found with respect to his reforms that were initiated back in, I think, 1981?

Mr. BOWSHER. We did discuss the importance of the main issues that I raised today. Two things that we discussed a great deal with Carlucci at that lunch were the need for stability at the Defense Department and the management of DOD—you have to have an information flow coming back up. You can't run the Department if you don't have the information. And a third thing was this issue involving the defense contractors themselves. I told Secretary Carlucci that everybody who has ever gone to bat for the defense contractors as far as relaxing oversight has generally ended up with egg on their face. And I said one more time it is happening here, and you have to get tough. I think somebody has to get tough with the contractors and say that we were going to hold the top leadership of these major corporations responsible for what is happening. The contractors have to get rid of these sleazy consultants or anybody else who does not meet ethical standards. The idea that the top people don't know what's happening—what you have to get across—that that's not an allowable excuse in the future.

And I also discussed with him the issue we had in the early 1970s involving sensitive payments. I said that's when you finally got the top people in and told them that they had to cut this out.

Senator COHEN. What do you mean by sleazy consultants? [Laughter.]

We have some pretty qualified people who leave the military, generals, two, three star generals go out.

Mr. BOWSHER. I'm thinking of the ones that violate their trust.

Senator COHEN. Well, let me just give you an example of what happens. You have very qualified people who serve their full 20, 25 years or more in the military. They leave. They set up a consulting firm. I can think of a half dozen, maybe more, off the top of my head who form consulting firms, somebody from the Army, someone from the Air Force, someone from the Navy. They go into business. They approach various corporations who are building these systems. These companies, in fact, turn to those individuals for the very reason that everybody understands why they are turning to them because they have access to the Pentagon.

And then there is pressure on them saying, look, we're paying you a pretty high fee. We read in this morning's paper where one individual went from rags to riches rather quickly. We're paying you a pretty high fee, and you've got to produce. And so, the pressure is on at that point for them to produce any which way they can, and the way in which they choose to do so is to go back into the bowels of the Pentagon.

So, how do you determine what's a sleaze operation and what's a quality consulting operation?

Mr. BOWSHER. I think a quality operation would be one that was giving you some technical advice, let's say, on radars or something like that. You hired them because you needed that kind of expertise, and you weren't applying the kind of pressures that you described, Senator. But I think the situation that you described is what a number of them have turned out to be.

I think your description also indicates that the companies, to a great extent, are putting this pressure on. It isn't just the consultant. There's a lot of thinking right now that if we just get a few bad consultants out of the game, we will be in good shape. I think you have to look at those companies.

Chairman NUNN. You've stated, Mr. Bowsher, that the current procurement problems underscore the importance of government oversight and management attention on a continuing basis. Is this a scenario in which we need more audit and oversight resources or more improved management or a combination?

Mr. BOWSHER. I think primarily management. In other words, one of the things I would do, which is getting kind of a technical approach, but I would tie in the CPA audits more to the audit committees. I don't think you have to go out and hire thousands of auditors for the Defense Department or anything like that. I think you've got large staffs. Industry has been making a lot of noise recently about too many audits—I don't believe that's true. I think you need an effective audit program, but the thing you need most is management, and you need that on the Government side and you need it on the private sector side.

Chairman NUNN. Would you explain that audit? You just mentioned the CPA audit.

Mr. BOWSHER. Yes. What the SEC decided last week was to take up the recommendations of what is known as the Treadway Commission. The Treadway Commission came out of the Dingell hearings of a couple years back where they were claiming that there were too many cases of fraud, like ESM, that were taking place where the auditors didn't catch the fraud. The auditors didn't report the fraud before it happened. So, the commission said that the CPA firms ought to be spending more time and attention looking for fraud as they do their annual audit.

Chairman **Nunn**. You mean the CPA firms hired by the private contractor.

Mr. **Bowsher**. That's right, who do the annual audit and whose certification is in the annual stockholders report.

Now, the CPA firms are not anxious to take on that responsibility because they only perform a random sample of their testing and review. They don't want to be responsible for every possible fraud. But the courts are holding them to a higher level of responsibility.

What has happened now—and I think it is a very good development—is that the SEC is coming out with a rule that management ought to issue a statement once a year as to what they believe is the state of their controls in their company. The CPA firm then ought to review that statement and say whether they, based on their audit, found any additional weaknesses. Then management must also say what they plan to do to correct the weaknesses. The auditing firm ought to say whether that plan is adequate to correct the weaknesses.

I think at that point not only are you getting management involved, you're getting an outside group involved, and you're involving the audit committee of the board of directors. So, you are really getting the top people involved.

I think if that passes, if the SEC puts that in as a final ruling, then the Defense Department could take that, maybe add even a few things that are unique to defense contracting, and make that part of the corporate governance principles or ethics. It would have a lot more teeth in it than just having a booklet. In other words, a lot of companies have produced some good booklets, but obviously from what has happened with these scandals, some people in the corporations have been able to violate the standards. I worry when I see vice presidents and people at that level involved, if that is what the allegations finally prove. I think you have to get senior management, the CEO, the board of directors, the audit committees involved in addressing this overall issue.

Chairman **Nunn**. There have been several allegations about source selection. Just for the record here—I think some of this is obvious and common sense, but I think it would help our record if you gave us your view of the effect on our national defense in terms of price and capability and so forth, the national defense requirement. Let's take two or three things.

Number one, improper disclosure of information. Now, what's the effect on the bidding process when information that is not supposed to be disclosed is disclosed to competitors?

Mr. **Bowsher**. Well, the effect that you can have is that you might be paying more than you should, more of the taxpayers' money for the weapon. Second, you might get a contractor that under a fair and impartial process would not have won, and theoretically the contractor that won through fraud might not have the best weapon. So, you might have the wrong product, the wrong contractor, and be paying too much for it.

Chairman NUNN. What about collusion in bidding between contractors? What is the effect of that?

Mr. BOWSHER. I think the same is true. If you have collusion, you could end up with some combination of contractors winning that shouldn't have won.

Chairman NUNN. And the same thing would generally be true in terms of rigging specifications to favor one contractor?

Mr. BOWSHER. That's right.

Chairman NUNN. Is there a case to be made that there is too much restriction on proprietary data and that the Department of Defense ought to be able to more freely exchange proprietary data between contractors?

Mr. BOWSHER. I know people have alleged that. But it's really the proprietary data that seems to be involved in this, plus the price. So, I'm not sure—there might be some merit in that, but right now we're not prepared to say.

Chairman NUNN. Are you looking at that or will you be looking at that as to what is disclosed and what should be disclosed?

Mr. CONAHAN. That becomes part of the ongoing criminal investigator with respect to these specific cases. I think in keeping with your charge, we would want to stay away from that, but in a general sense, yes, sir.

Chairman NUNN. As the cases come in, you could monitor that, as the cases are completed.

Mr. BOWSHER. Yes.

Chairman NUNN. Senator Exon.

Mr. BOWSHER. Mr. Chairman, if I could just add one thing that I haven't covered today and it goes back 10 years to when my predecessor was in office, Elmer Staats. There was a lot of concern by State and local government that there was too much auditing by the Federal Government. And the GAO did a study and pretty much confirmed what they thought.

What evolved was known as a Single Audit Act which Congress passed 2 or 3 years ago after we tried it out on a prototype basis in several places. That act tries to get the CPA firms involved in doing certain things as they do that annual financial audit. Then when the Government auditors come in, they build on what is really done. It has already been accomplished.

I think that's something that ought to be given some thought here because obviously industry is complaining about too much audit. It may be a case of where some different approach to auditing could be tried. Then if it looks like it has some merit, it could be adapted for the defense industry. I think you have many of the same attributes where large chunks of Federal money are going out into the private sector or to another level of government.

Chairman NUNN. Thank you very much.

Senator Exon.

Senator EXON. Thank you, Mr. Chairman.

I just have one question, Mr. Bowsher, and I thank you for your excellent testimony today which I think has been very helpful to all of us. Let me go back to this best and final offer proposition a little bit.

In your opinion is this overused at times? It seems to me that we have created a situation, while a best and final offer may be entirely proper in some instances, to have that pretty much a rule of thumb opens up the possibility for the kinds of wrongdoing that evidently have happened now. Is the best and final offer proposition used too often in your opinion? Is there a possibility that maybe we have relied on that too much in some instances which has contributed to this leak, all the shenanigans that evidently have been going on at least in some areas? What about best and final offers?

Mr. **Bowsher**. I served on an advisory committee to the Deputy Secretary of Defense in the mid-1970s when I was out of Government and back in the private sector. This was an area that we studied quite a bit. We came to the conclusion at that time that it was overused. We didn't zero in so much on the potential for scandal, but we did zero in on the issue of fairness. As we do this procurement study in the next few months, we will look again at this.

But I think the potential for problems, as you describe it, is there. If it is being used too much, which it might well be, then that is probably one of our problems.

Senator **Exon**. You don't have any offhand opinion now of whether it is being used——

Mr. **Bowsher**. No, I don't offhand.

Senator **Exon**. I'm very glad that you're going to look into that, and I'll look forward to reading that when you come out with it.

Thank you, Mr. Bowsher. Thank you, Mr. Chairman.

Chairman **Nunn**. Thank you.

Senator Bingaman.

Senator **Bingaman**. Mr. Bowsher, I wanted to go to one of the points in your testimony. You sort of went past it because it is not the direct subject of this hearing. But you said: "I think the other shoe will probably fall soon, namely, many big cost overruns. I suspect the Stealth airplane program, the Navy shipbuilding program and other programs which have to be stretched because of budget constraints will all result in very large cost increases that the Congress and the taxpayer will have to finance."

Could you elaborate a little bit and tell me—you mentioned Secretary Laird saying he wanted all the bad news and wanted to know how many more of these things like the C-5 were in the building. What does Congress have to do to regularly hear what the real story is on some of these programs? I mean, we are making decisions here on an ongoing basis on one set of assumptions, and you're saying that that set of assumptions probably is not right with regard to a lot of these programs?

Mr. **Bowsher**. The system that was set up right after that by Secretary Laird was a system that was being prototyped, as a matter of fact, by McNamara, and that was known as the SAR reports. Those do flow regularly to the Congress. But I believe they have deteriorated terribly. In other words, I don't think the reports are very good at all. And there has been efforts over the years to improve these reports. In fact, Congressman John Spratt of South Carolina is one who is very interested in this because he served at the Department of Defense when they were initially implemented. That is the system that could do the job. If the Department of Defense were willing to come up with honest, realistic reporting and estimates and get the industry information flowing into it properly, the mechanism is there.

Senator BINGAMAN. You say the other shoe is going to fall soon. When do we get the message on these programs?

Mr. BOWSHER. I suspect you'll start getting it when the new administration comes in.

Senator BINGAMAN. I see. No way to get it before the end of the year.

Mr. BOWSHER. If the present Secretary of Defense made a major effort to see if he has more problems than his reports are indicating, you might be able to get it. That's what I'd go after.

Senator BINGAMAN. There is nothing that you're doing that will shed light on this in the coming months.

Mr. BOWSHER. No. We are doing work on some of the major weapons, but the better approach would be to do just what Laird did—demand from the system where we really stand on these systems now. I think your committee especially needs it now because if you don't have realistic cost estimates, you're going to get a set of program decisions that later will not be able to hold up.

Senator BINGAMAN. So, you're saying we need to press the Secretary to give us that information before we get into the next budget cycle.

Mr. BOWSHER. I think so.

Senator BINGAMAN. That's all I had, Mr. Chairman.

Chairman NUNN. Mr. Conahan and Mr. Hinchman, do you have anything you'd like to add today? I know both of you are real experts in this area, and we appreciate your professionalism and all you've done over the years. Do you want to add anything that comes to mind?

Mr. CONAHAN. I think, Mr. Chairman, that the issues that we need to deal with have been aired very well this afternoon. I really don't have anything to add. Thank you.

Chairman NUNN. Mr. Hinchman.

Mr. HINCHMAN. No. Mr. Chairman. I think that Mr. Bowsher has covered everything.

Chairman NUNN. We could stipulate that the boss is perfect, but now do you have anything? [Laughter.]

We appreciate all of your being here. It has been very, very helpful to us and we will have a continuing dialogue with you and be relying on you very heavily as we go through this.

Also, as these possible suspensions come up, if you could have some people that would be right on top of that because the question of whether we suspend certain contractors, whether certain people are disbarred, we are going to need oversight over that process. Of course, the primary decision makers have to be the Department of Defense, but we will need your advice.

Mr. BOWSHER. We'll do it.

Chairman NUNN. Thank you.

[Questions for the record with answers supplied follow:]

QUESTIONS SUBMITTED BY SENATOR SAM NUNN

Senator NUNN. Mr. Bowsher, your statement notes that many defense contractors are subject to the provisions of the Security and Exchange Act's recordkeeping and internal accounting control requirements, but that these provisions do not specifically cover cost, price, estimates, billing, and performance management controls. You also noted that recent SEC initiatives begin to address some of these provisions. Please describe the purpose and requirements of current law, the SEC initiatives, and your assessment of the effectiveness of these initiatives is promoting effective internal accounting controls.

Mr. **Bowsher.** Currently the provision of the Foreign Corrupt Practices Act of 1977 have a bearing on corporate internal accounting controls and associated record keeping requirements. The Act specifies that every issuer of securities covered by the Act shall devise and maintain a system of internal accounting controls sufficient to provide reasonable assurance that transactions are properly recorded and assets are adequately safeguarded.

The current SEC initiatives on this topic can be traced to the October 1987 Report of the National Commission on Fraudulent Financial Reporting (Treadway Commission). The Commission has recently approved for issuance a proposed rule dealing with issues in this area. The proposed rule would require managment to submit a "management report" that would "acknowledge management's responsibilities for the financial statements and internal control, discuss how these responsibilities were fulfilled *and provide management's assessment of the effectiveness of the registrant's internal controls.*" The publication of this proposed rule is expected in the near future. Auditors of those public companies should be expected to perform a review and evaluation of this management report on controls.

We believe that the SEC initiatives in this area will enhance the quality of internal control particularly as applied to data employed in the preparation of annual financial statements. However, the impact of these initiatives will be somewhat more limited when applied to contract specific data including contract costs, price, estimates, billings and performance measurement controls. The primary focus of SEC is on corporate financial reporting and not on contract specific data. The focus on contract specific data could be expanded by incorporating more specific guidance on these areas in the AICPA Industry Audit Guide and through the Contractor Risk Assessment Guide program currently being evaluated by DOD.

TRUTH IN NEGOTIATIONS ACT

Senator **Nunn.** Your statement notes that GAO's studies have "consistently shown that contractor compliance with the (Truth in Negotiations) Act falls short of full disclosure." Please describe the purpose and requirements of the Act, the results of GAO's reviews, and any recommendations that you might have for improvements in compliance with the Act.

Mr. **Bowsher.** The intent of the Truth in Negotiations Act (P.L. 87-653) is to place the government on an informational parity with contractors so that both parties have the same information for negotiating fair and reasonable prices on noncompetitive contracts. The Act requires that, with certain exceptions, contractors submit cost or pricing data in support of proposed prices for noncompetitive contracts. Contractors are also required to certify that data submitted are accurate, complete, and current. Where P.L. 87-653 is applicable, a clause is included in the contract which gives the government a right to a price reduction if it is determined that the price was defective because the data submitted were not in accordance with the statute and the certification.

GAO INVOLVEMENT

Based on congressional concerns, we have devoted considerable resources to contract pricing reviews with heavy emphasis on defective pricing audits. Since May 1986, we have issued 19 reports recommending recoveries of $32.1 million. The reports are based on reviews performed at both prime and subcontractor locations where we found nondisclosure of more current information such as vendor price quotations, actual subcontract awards, or lower direct labor rates. Currently, we are performing defective pricing reviews at seven major defense contractor locations and we will continue to perform such reviews.

IMPROVING CONTRACTOR COMPLIANCE WITH THE ACT

Congress recently revised the Truth in Negotiations Act to more adequately protect the government's interests. In particular, Congress more clearly defined cost of pricing data, eliminated certain contractor defenses, clarified the issue of "offsets" against recovery for defective pricing, and imposed interest and double damages for overpayments by the government.

We support these revisions and amendments and we believe the most effective means of ensuring compliance with the Act is through continuous audits at defense contractor locations.

Senator NUNN. During your testimony, you expressed concern that agency compliance with the reporting and evaluation requirements of the Federal Managers' Financial Integrity Act has become a mere paperwork drill. Please describe the purpose and requirements of the Act, give your assessment of DOD's implementation of the Act, and any recommendations you have to improve compliance with the purposes of the Act.

Mr. BOWSHER. The purpose of the Federal Managers' Financial Integrity Act is to reduce fraud, waste, and abuse, and to improve management of federal operations by strengthening agency internal control and accounting systems. The Act requires that each executive agency evaluate its systems of internal control on an ongoing basis. It also requires the agency head to annually report to the President and the Congress on whether the control systems meet the objectives of controls cited in the act and comply with the internal control standards prescribed by the Comptroller General.

Overall, I believe DOD has in place the processes and procedures necessary for implementing the Act's requirements and that these mechanisms have resulted in the identification and correction of a number of significant management control weaknesses. For example, from 1983 to 1987 DOD has reported 382 control weaknesses. Of this number they report that 279 (73 percent) have been corrected. I believe this represents good progress. However, our work in certain program areas does raise some reason for concern. For example, our work has shown instances where (1) material weaknesses existed but had not been reported (*Army Inventory Management: Inventory and Physical Security Problems Continue,* GAO/NSIAD-88-11), (2) material weaknesses which has been reported as corrected still existed (*Controls Over Expedited Payments to Defense Suppliers Need Improvement,* GAO/NSIAD-88-113), and (3) inadequate internal controls for a major activity (*Strategic Defense Initiative Program: Better Management Control and Direction Needed,* GAO/NSIAD-88-26).

I do not have any proposals specifically for the DOD at this time. However, I do believe that the Act's government-wide implementation can be improved by (1) OMB issuing more definitive guidance on the definition of materiality (OMB is currently working on this) and (2) internal and external audit activities doing a better job of assessing management controls and identifying to management those control weaknesses which should be reported to the President and the Congress. Lastly, I feel strongly that the key to successful implementation of the Act in DOD as well as in other federal agencies is senior management commitment to the identification, disclosure, and correction of control weaknesses.

DISCLOSURE OF SOURCE SELECTION INFORMATION

Senator NUNN. The public information on allegations now under investigation has focused on disclosure of information during the source selection process. In the conduct of competitive negotiations, discussions between the government and potential offerors are an integral part of the process. Has the Department of Defense developed useful criteria for distinguishing between the types of source selection information that should be disclosed and the information that should be secured, or is this left primarily to the discretion of individual contracting officers?

Mr. BOWSHER. Procurement regulations applicable to the Department of Defense (DOD) contain useful criteria concerning disclosure of information in connection with competitively negotiated procurements. Section 15.610 of the Federal Acquisition Regulation provides that during discussions a contracting officer must (1) inform an offeror of deficiencies in its proposal so that the offeror is given an opportunity to satisfy the Government's requirements, (2) attempt to resolve uncertainties in the proposal, and (3) advise the offeror of suspected mistakes without disclosing information concerning the proposals of the other offerors or the evaluation process. Furthermore, the contracting officer may not disclose technical information contained in competing proposals, advise offerors of the relative standing of their price proposals, or otherwise furnish information about other offerors' prices.

The regulations also (1) require that proposals and quotations received from offerors be safeguarded from unauthorized disclosure and (2) certain restrictions on who may transmit information to and conduct discussions with prospective contractors. In addition, FAR 15.612(e) requires that, whenever a formal source selection process is used, (1) particular care be exercised to protect source selection information on a strict need-to-know basis, (2) during the selection process, approval by the source selection authority is required before any release of source selection data, and (3) Government personnel "shall not contact or visit a contractor regarding a proposal under source selection evaluation, without the prior approval of the source selection authority."

Senator NUNN. Should consideration be given to promoting greater sharing of information during competitive negotiations, with prohibitions on disclosure apply only to proprietary data and cost proposals?

Mr. BOWSHER. As a general rule, the Government relies on the competence and inventiveness of the individual offerors to structure proposals responsive to the Government's requirements. Sharing of information among the offerors is not a practice the Government uses. Disclosure of ideas and approaches contained in competing proposals could operate in the long run to discourage the very creativity on the part of offerors that the Government seeks to promote.

DEFRAUDING THE GOVERNMENT

Senator NUNN. The Under Secretary of Defense for Acquisition recently said: "Our acquisition system works. Otherwise, we wouldn't be able to identify persons who attempt to circumvent it? They may elude us for a while but, in the end, we prevail." Based on GAO's review of DOD's oversight of contractors, do you agree with the Under Secretary's assessment that it is as difficult to defraud the Government—and get away with it—as the Under Secretary has suggested?

Mr. BOWSHER. Because fraud is not easy to detect, we do not believe anyone really knows how much fraud is committed against the Government. We are convinced, however, that reliance solely on Government efforts to detect and prosecute fraud is destined to fall short of the goal of eliminating fraud from the procurement system. The contractors themselves, particularly top management, must be fully committed to and involved in achieving that objective. Both the Congress and GAO have encouraged improved internal management control systems, which are a primary deterrent against and aid in detecting fraud. Improvement in this area remains a necessity.

FRAUD REMEDIES AVAILABLE TO THE GOVERNMENT

Senator NUNN. Please describe the remedies that are available to the Government in the event of fraud. In your discussions, please distinguish between those remedies that involve termination of the contract and those remedies that can be taken when Government decides that it is in the national interest for the contract to be completed.

Mr. BOWSHER. Subpart 3.7 of the Federal Acquisition Regulation provides that where there has been a final conviction by a court for bribery, conflict of interest, or similar misconduct in connection with a Government contract, the Government after notice and hearing may declare the contract void for cause and recover amounts it has expended, less the fair value of the property received and accepted by the Government.

Under the gratuities clause of a Government contract, the Government may terminate the contract for cause if, after notice and a hearing, the Government determines that the contractor or its representative offered or gave a gratuity to a Government employee in order to obtain a contract or favorable treatment under a contract. The clause provides that the Government is entitled to (1) pursue the breach of contract damages, which may include reprocurement costs and other damages as appropriate, and (2) receive exemplary damages of not less than three nor more than ten times the amount of the gratuity.

Finally, under the termination for convenience clause the Government has the right to terminate a contract at any time, but the contractor is entitled to be paid for preparations made, work performed, profit on that work, and settlement expenses.

In the event the Government desires continued performance of a contract tainted by fraud, the Government may be entitled to recover damages from the contractor to the extent that the fraud caused the contract price to be overstated. The Government may also take appropriate action against individuals involved and, with respect to future contracts, may initiate suspension or debarment proceedings against the contractor.

FRAUD REMEDIES AVAILABLE TO DISAPPOINTED OFFERORS

Senator NUNN. Please describe the remedies that are available to disappointed offerors in the event of fraud. In your discussion, please cover the rights, if any, that a disappointed offeror would have against the Government, and the impact of any remedies on the performance of contracts.

Mr. **Bowsher**. A firm that is denied a Government contract due to fraud may seek to have the award overturned by filing a protest with GAO (or with the General Services Administration Board of Contract Appeals for automatic data processing procurements), provided such a protest is filed within 10 working days of when the protester knew or should have known the basis for its protest. If the protest is filed with GAO within 10 calendar days of the award, the contracting agency normally must direct the awardee to cease performance of the contract pending a decision on the protest. Possible remedies for successful protesters to GAO or the GSA Board include (1) award of the contract to the protester, (2) recompetition of the contract, or (3) reevaluation of the proposals. If none of these remedies is appropriate, the protester may be able to obtain its bid or proposal preparation costs and costs of filing and pursuing the bid protest.

A firm may also protest to the procuring agency or it may go to court and seek judicial remedies.

CENTRALIZED ACQUISITION AGENCY

Senator **Nunn**. GAO has examined the concept of a centralized acquisition agency. What are the advantages and disadvantages of such a concept, as compared to the present division of responsibility between OSD and the services?

Mr. **Bowsher**. The fiscal year 1986 Defense Authorization Act required GAO to review all available reports and analyses of the organizational structure for defense procurement and report on the advantages and disadvantages of establishing a centralized civilian acquisition agency. In responding to this requirement, we reviewed reports and analyses and sought the views of DOD military and civilian officials involved with the acquisition process, individuals in the defense industry, members of academia and recognized defense experts.

Our report, *Advantages and Disadvantages of a Centralized Civilian Acquisition Agency* (GAO/NSIAD-87-36), issued in November 1986, identified some of the more significant advantages of this concept as:

—Reducing service parochialism, thereby creating an environment for more common or joint weapon system development;

—Improving the quality and continuity of the acquisition work force; and

—Reducing the acquisition work force and administrative layers by consolidating duplicative and overlapping acquisition functions.

Some of the more significant disadvantages identified were:

—Acquisition problems were not necessarily organizationally related and no single action, such as establishing a centralized civilian acquisition agency, would solve them;

—The military's operational experience, which lends credibility that new equipment is operationally suitable and effective for military use, may not be available if a purely civilian organization were established; and

—The potentially large size of the agency work force and organization would create an unusual management challenge, and could be unmanageable.

While we did not express an opinion on establishment of such an agency, our report noted that the predominant views expressed by those we contacted were against establishing such an agency. Most believed that any advantages offered would be more than offset by the disadvantages.

QUALIFIED ACQUISITION PERSONNEL

Senator **Nunn**. You have emphasized the importance of filling acquisition positions with qualified personnel. What changes in the existing personnel system would you recommend to achieve this goal?

Mr. **Bowsher**. In our 1986 report, *Strengthening Capabilities of Key Personnel in Systems Acquisition* (GAO/NSIAD-86-45), we examined the capability of the defense acquisition work force. We made several recommendations for changes to the existing DOD acquisition personnel system.

To better define the acquisition career field and the requirements for advancement within it, we recommended that:

—The service Secretaries establish career fields or functional specialties in acquisition management, define desired acquisition experience within these career fields, and provide personnel with adequate acquisition experience.

—The service Secretaries select program managers based on their performance in the acquisition career field.

—The Secretary of Defense develop specific education, experience, or other selection criteria for system contracting officers based on their roles and responsibilities.

In its response to the recommendations in our report, DOD stated that the Secretary of Defense issued DOD Directives 5000.23 and 5000.48 in December 1986 addressing DOD acquisition career fields.

The directives define career fields for and responsibilities of program managers, program management support personnel, contract negotiators, contract specialists, and contract administrators, as well as personnel in other related acquisition fields. The directives also specify training, experience, and educational requirements for various levels of military and civilian acquisition personnel. In addition, Directive 5000.23 provides policy for the selection of program and deputy program managers.

We are currently planning a follow-on effort to the above cited report in an attempt to determine what further actions DOD could take to strengthen the acquisition workforce.

Additional recommendations made in our 1986 report include the following:

—DOD should assign program managers and contracting officers at the conception stage of major weapon programs.

—Each program office should have a clear focus and responsibility for contracting strategy formulation and execution. The contracting officer or other expert filling such a position should be a highly qualified system acquisition expert and a full team member from inception of the program.

—The service Secretaries should identify types of program manager positions for which civilians should be considered.

—The Secretary of Defense, after clarifying contracting officers' roles and responsibilities and fully establishing the program office team approach, should provide career incentives for system contracting personnel by allowing them to enter other acquisition fields through development and opportunity.

Senator NUNN. What are the advantages and disadvantages of creating an Acquisition Corps without its own separate personnel system?

Mr. BOWSHER. It is not clear that a new personnel system would be essential to accomplish the desired objectives. Enhanced training, greater accountability for job performance, and more stringent qualifications criteria for entry into the acquisition field are all possible under the current system.

The major deterrent to getting top people into federal service may be the large gap that has been allowed to develop between federal and private sector salaries. DOD can request special pay rates from the Office of Personnel Management for employee groups in specific localities or nationwide when employing agencies can demonstrate that they are unable to recruit and retain quality personnel because of higher private sector pay.

If the pay rates available under this mechanism are not sufficient to resolve recruitment and retention problems, changes to the current personnel system could provide several advantages over the existing system, such as:

—Adoption of broad-band job classifications in lieu of the narrow job classifications under the current General Schedule. This could increase managerial flexibility in staff assignments and increase the pay ranges for some employees.

—Authorization of relocation expenses for the first post of duty. Current regulations permit such expenses for "shortage category" jobs only.

—Implementation of geographic pay rates to recognize regional cost-of-living and private sector pay differentials. The current federal pay system provides national pay rates, regardless of locality, to all employees, except where special pay rates are authorized. Cost-of-living allowances are now permitted only for employees in Alaska, Hawaii, Puerto Rico, the Virgin Islands, and overseas locations.

—Authorization of recruitment bonuses for hard to fill positions. Current regulations do not allow recruitment bonuses.

—Reimbursement of employee college expenses or scholarship grants. Current regulations do not permit payments to employees to obtain college degrees.

Care needs to be taken in any actions to address problems in the recruitment and retention of DOD acquisition personnel. Establishing a separate system for DOD acquisition personnel alone could be inequitable to acquisition personnel in other agencies as well as other types of personnel experiencing similar conditions.

ACADEMIC PREPARATION

Senator NUNN. There are relatively few schools of law, business, or public administration that offer degrees in acquisition management or contract law. What, if anything, can the government do to encourage academia to prepare students for careers in government service related to the acquisition process?

Mr. **Bowsher**. I believe that a solid foundation for later training and careers related to the acquisition process needs to be provided by our colleges and universities through their undergraduate and graduate business and law programs, and I fully support such educational programs for individuals hoping to specialize in federal acquisition management.

In developing our previously mentioned 1986 report (GAO/NSIAD-86-45), we discussed with experts within and outside of DOD the type of educational backgrounds which would best prepare contracting officers for their responsibilities. They state it would be desirable for contracting officers involved in major systems acquisition to be familiar with such issues as competition, structure of the marketplace, analytical models, computer technology, business strategies, and accounting. These skills and issues are normally available in a business curriculum, and experts viewed a business degree as desirable educational preparation for a weapon systems contracting career.

It should also be noted that many of the positions in acquisition require a strong technical, rather than business, background. A degree in such fields as engineering or physics is considered essential for many acquisition management positions.

The Federal Government should take the lead in providing adequate on-the-job training, specialized classroom instruction, and career opportunities for the college graduates it hires as acquisition specialists. This arrangement is necessary for the new employees to learn the intricacies of the ever changing acquisition statutes, regulations, policies, and procedures.

The Packard Commission's 1986 report recommended that federal law should permit expanded opportunities for the training and education of civilian acquisition personnel. Following that recommendation, Congress, through the title IX of Public Law 99-661 (The National Defense Authorization Act of 1987), required the Secretary of Defense to develop a plan for enhancing the professionalism of, and career opportunities available to, DOD acquisition personnel. In May 1987, the Secretary of Defense submitted the plan. As part of this plan, the Office of Personnel Management is in the process of establishing a requirement for 25 hours of college level business management-related courses to enter the 1102 contracting series.

NEED FOR PRIOR ACQUISITION EXPERIENCE

Senator **Nunn**. Can the key acquisition positions in the Department of Defense, such as the Under Secretary for Acquisition, the Service Acquisition Executives, and the functional Assistant Secretaries be filled with persons who receive "on-the-job" training in the government's acquisition process, or are these jobs in which persons should have demonstrated relevant experience in Government and industry?

Mr. **Bowsher**. Without question, the demands placed on DOD's top procurement officials are such that management skills and prior experience with the Government's acquisition process, obtained either in-house or with industry, are important. The responsibilities of thse offices cannot be discharged effectively by individuals who would receive only "on-the-job" training. Acquisition is a complex process, issues and problems must be dealt with on a daily and continuing basis. Therefore, it is important that individuals selected for these key positions possess the knowledge, skills, and abilities to manage the acquisition process.

QUALIFICATIONS FOR SENIOR ACQUISITION EXECUTIVES

Senator **Nunn**. What advice would you give the next President in terms of the qualifications that should be established for selection of persons to serve as the Under Secretary for Acquisition and as the Service Acquisition Executives?

Mr. **Bowsher**. These key positions require individuals who are, first, effective and proven managers; second, experienced in and knowledgeable about the Government's acquisition process; and third, knowledgeable about weapons acquisition. In addition, I believe it is essential that the Secretary of Defense be able to name his own management team. This team must share and continually work toward a common set of goals and objectives. This cannot be done without extensive coordination and cooperation among the key managers. The Secretary needs a management team of individuals that are not only experienced, but also capable of working together to make the difficult decisions that are required.

SERVICE ACQUISITION EXECUTIVES

Senator **Nunn**. The Packard Commission recommended that each service have a full-time Acquisition Executive. The Air Force is the only Military Department with a full-time Service Acquisition Executive. The Army and Navy have designated their Under Secretaries to serve as the Acquisition Executive. The Under Secretary, of course, must also serve as the Service Secretary's alter ego on a wide variety of matters unrelated to acquisition. Is it possible to implement the structure envisioned by the Packard Commission with a part-time Acquisition Executive?

Mr. **Bowsher**. I believe there should be a full-time senior official dedicated to weapon system acquisition. However, it may be appropriate to designate the service Under Secretary as the Service Acquisition Executive in order to facilitate oversight over a broader range of acquisition functions including the acquisition of information systems and logistics-related acquisition activities. For example, the logistics-related acquisition activity may come under a deputy chief of staff and direction and oversight may be more appropriately provided at the Under Secretary level. Further, designation of the Under Secretary of Service Acquisition Executive is consistent with the designation of the Under Secretary of Defense as the Defense Acquisition Executive.

DUPLICATIVE OVERSIGHT

Senator **Nunn**. You have stressed the importance of vigilant oversight to assure that industry institutes needed internal control measures. At the same time many observers, including the DOD Inspector General, have noted that the Department's efforts are plagued by unnecessary, duplicative oversight activities. What steps can the Department take to ensure that its oversight resources are used efficiently and not squandered on repetitive, duplicative reviews.

Mr. **Bowsher**. The Packard Commission advanced the idea of contractor self governance to help relieve excessive oversight. Properly applied, I believe this concept can reduce oversight and at the same time preserve the integrity of the system, which is necessary to be fully accountable to the public trust. DOD is developing a Contract Risk Assessment Guide (CRAG) program which is in the spirit of contractor self governance to reduce duplicate oversight. This program is designed to improve the effectiveness and efficiency of DOD oversight. The overview of the program states that: "Contractors who can demonstrate the implementation of internal control systems that meet CRAG control objectives will receive less direct government oversight. By assessing the validity of contractor internal control systems, the extent of government oversight can be reduced, thereby enabling DOD to concentrate its oversight resources on known problem areas."

Although the CRAG program is in the early stages of development, full implementation of its objectives could contribute to reducing oversight and improving the effectiveness and efficiency of DOD oversight.

Another program which could assist in a move toward effective self governance is one which was recommended by the Treadway Commission and is currently being studied by the Securities and Exchange Commission. This program calls for management reviews of internal company controls to be performed by audit committees of the Board of Directors. These reviews would be followed by annual management statements on the companies' internal control systems. The certified public accountant (CPA) firms that annually audit the companies' financial statements would review the management statements and say, based on their audits, whether they found any weaknesses in the control systems. This program sounds promising.

GAO has long been an advocate of eliminating duplicative oversight where such duplication can be removed without peril to the proper disbursement of public funds. Several years ago GAO sponsored legislation which resulted in the Single Audit Act (Public Law 98-502). This law provided for single audits of federal grants to state and local governments. This was a significant step in eliminating duplicative oversight at the state and local level. We believe this same concept should be looked at to see if it can be applied to elements of the defense procurement process.

On April 14, 1988, we testified before the Senate Subcommittee on Defense Industry and Technology on the proposed Defense Industry and Technology Act of 1988. To deal with concern over duplication in audit and oversight, the bill would require (1) an annual plan for audit and oversight functions and (2) the Under Secretary of Defense for Acquisition to report DOD's progress in preventing oversight duplication.

As we stated in that testimony, we support a coordinated plan for audit and oversight activities and believe that such an approach should help avoid duplication. The DOD Inspector General, the Defense Contract Audit Agency, and other internal audit agencies currently prepare and coordinate annual audit plans. In fact, the Defense Acquisition Improvement Act of 1986 requires that the Under Secretary, in consultation with the DOD Inspector General, prescribe policies to prevent duplication.

New final rules issued in Federal Acquisition Circular 84-37 contain a provision designed to curb duplicative audits of contractors. To determine whether the information requested by a prospective visitor to a particular contractor has recently been reviewed by or is available from the government, this Federal Acquisition Regulation revision requires the contract administration office to consult with the contractor and the cognizant audit office. If appropriate, the contract administration office is required to "discourage the visit" and refer the visitor to the government office where the data are available.

The fiscal year 1989 Defense Authorization Bill, vetoed by the President on August 3, 1988, included a provision requiring DOD to prepare a report assessing the feasibility and desirability of requiring that no DOD oversight entity may review an activity if another entity has reviewed it within the past year. The bill would also require DOD to coordinate annual audit plans developed by DOD components.

DEFENSE PROCUREMENT FRAUD UNIT

Senator NUNN. To what extent does your critique of the Defense Procurement Fraud Unit reflect problems that the Department of Justice has encountered in attracting and retaining experienced attorneys knowledgeable in the procurement laws? What can be done to address this problem?

Mr. BOWSHER. As indicated on pages 26 and 27 of our report (GAO/GGD-88-96), the Chief of Justice's Defense Procurement Fraud Unit and managers and/or attorneys at several U.S. attorney offices we visited said that turnover among attorneys as well as support staff has had an impact on their prosecutive effort. According to these officials, the primary reason for staff turnover is the higher salary structure available to the attorneys and support staff in the private sector.

Practical solutions to this problem are not readily apparent. Justice officials told us that many attorneys join the Department to gain trial experience and intend to stay only a few years. Although this matter is not specifically addressed in our report, one possible approach is for Justice to develop better incentives, both monetary and nonmonetary to (1) encourage experienced attorneys knowledgeable in the procurement laws to remain with the Justice Department and (2) attract new experienced attorneys to the Department.

DEFENSE-JUSTICE RELATIONSHIP

Senator NUNN. Is the relationship between the Department of Defense and the Department of Justice on the investigation and prosecution of fraud structured in a manner that ensures timely and successful investigation of fraud allegations?

Mr. BOWSHER. GAO's review of Justice's management of the investigation and prosecution of defense procurement fraud did not address the structural relationship between the Departments of Defense and Justice. Consequently, we are not in a position to answer this question.

CONSULTANTS

Senator NUNN. Based on your review of DOD's use of consultants, to what degree has the Department relied on consultants to perform core government functions such as establishment of source selection criteria and evaluation of bids? Has DOD failed to provide adequate regulatory guidance to the Services or is this a problem of inadequate management attention?

Mr. BOWSHER. GAO has a review underway looking into the use of consultants on a government-wide basis. During this review, which is being conducted at the request of the Chairman of the House Armed Services Committee and Senator Pryor, we plan to address the questions you raise. We will look at the role of consultants through case studies of a specific weapon system in each of the military services and review DD's systems for monitoring and controlling the use of consultants. The work should enable us to comment on the specific roles consultants fill in each service, the adequacy of regulatory guidance, and the degree of management attention that has been given to the area. We should also be able to comment on differences in the manner and extent to which consultants are used in each of the services.

Questions Submitted by Senator Strom Thurmond

REGULATORY COSTS VERSUS BENEFITS

Senator **Thurmond**. Mr. Bowsher, there has to be a proper balance between industry and the Government. Industry needs to be regulated, but too much bureaucratic regulation can unnecessarily increase costs. How would you assess the balance in today's environment?

Mr. **Bowsher**. This is a difficult question because the proper balance is not easy to determine. Under Federal procurement laws and regulations, all capable contractors are permitted to compete to satisfy the Government's legitimate needs. Reliance on competition, at least partly, minimizes the need for other regulations and, at the same time, helps to ensure the fairness and integrity of the procurement process.

DOD reports that since fiscal year 1983 it has greatly increased the percentage of the value of its awards made competitively. However, DOD still awards many billions of dollars in contracts each year based on other than price competition. When contract prices are not based on (1) adequate price competition or (2) prices set by the commercial marketplace, then regulations are necessary to ensure the reasonableness of contract prices.

The question as to the proper balance between regulations and costs needs to be periodically reassessed as conditions change. We believe that key factors in reducing the reliance on regulations and the regulatory burden on contractors include public confidence in the integrity of the procurement process, including agency officials' compliance with competition requirements in law and regulations, and evidence of significant progress in the qualifications, training and professionalism of DOD's acquisition workforce.

PROCUREMENT REFORMS

Senator **Thurmond**. Mr. Bowsher, have various congressionally mandated reforms of the procurement process been implemented, and if so, have they been successful?

Mr. **Bowsher**. The DOD Authorization Act of 1986 contained more than 30 reform provisions for the defense acquisition process. The 1986 act was the latest in legislative reform measures dating from 1981 that affected almost every facet of the acquisition process. The vast majority of these reforms have been implemented. That is, regulations have been amended, new procedures have replaced cancelled ones, and organizational changes have been made. The reforms in general appear to have been successfully implemented. That is, if success is measured by reducing the costs of weapon programs, delivering the weapon systems on time, and the systems' performing as expected, then it would be correct to use the term improvement. However, the full effect of some of the reforms will take years to appear in the development, production, and the deployment of major weapon systems. With the number of reforms put in place over the past 7 years, the system needs a period of stability to see where we are and if more needs to be done.

CAUSE OF THE CURRENT PROCUREMENT PROBLEM

Senator **Thurmond**. Mr. Bowsher, in your opinion, is the current problem related to an absence of regulation and oversight, or human greed?

Mr. **Bowsher**. I believe that there is probably a little of both elements mentioned in your question in the current problems under investigation by the Department of Justice. Greed, of course, can be a powerful motivator. Other factors to consider are the enormous growth experienced in the defense budget over the past several years and a lack of adequate oversight over these expenditures. It is clear that more effective Federal oversight is essential.

As I mentioned in an answer to an earlier question, some additional oversight by companies themselves could help avoid these kinds of problems. For example, increased reviews of company internal control systems by audit committees reporting to the Boards of Directors, combined with annual management reports, could be a major step toward eliminating problems.

NAVY'S USE OF CONSULTANTS

Senator **Thurmond**. Mr. Bowsher, it has come to our attention that the Department of the Navy utilizes consultants to a far greater degree than the other services. Could you shed some light on this for the Committee?

Mr. **Bowsher**. As indicated in a previous response, GAO has a review underway looking into the use of consultants on a Government-wide basis. Based on this work, we should be able to comment on differences in the manner and extent to which consultants are used in each of the services.

THE DEFENSE MARKET

Senator THURMOND. Mr. Bowsher, the defense industry in this country can basically only sell to the Government. We do not sell defense material to the public, so the idea of competition is competition in a constrained environment. To what degree, in your opinion, does this lead to the sort of problem we are experiencing now?

Mr. BOWSHER. In general, the importance of DOD as the only buyer in the defense material market and the tremendous dollar value of its purchases, totaling about $160 billion annually in recent years, certainly create temptations for the unscrupulous to engage in unfair or fraudulent practices. However, DOD's importance in specific cases varies depending on the particular industry and the particular firms involved.

In general, a single buyer is in a position of strength relative to its suppliers, since they have no alternative markets. Two factors, however, can lessen the single buyer's bargaining position. First, if there is only one or a very small number of sellers, it is less clear where the balance of power in the relationship lies, because the buyer also lacks other alternatives.

Second, the buyer and sellers may not have the same information. In general, this is likely to occur in a situation in which the product being purchased has a large technical or innovative component, and it is difficult for the buyer to evaluate its true expected performance and risk characteristics. Such differences in information can persist throughout the demonstration and production stages of a product. The seller or sellers may have an incentive to avoid discussing questions of initial technical feasibility or the nature of any technical problems that may arise later in the process.

In addition to these general points, the following considerations are more specific to competition for large defense procurement contracts:

—The stage of the procurement process: The number of firms involved in a particular acquisition program often varies over the stage of the program, with some firms eliminated as the program progresses to the production stage. The incentives which firms face to participate in the process can also vary over that time. Firms have a tremendous incentive to participate in the research and demonstration stages of a program to qualify for work in the production stage. The extent to which involvement in these early stages alone is profitable varies, particularly if the firm has invested its own funds in the R&D work. If it has done so in the expectation of earning profits in the production stage, the firm's management is clearly under pressure to win a production contract.

—The size of procurement contracts relative to total revenues for the firm and industry: Firms that are largely dependent on DOD business have more to lose by failing to get a particular contract than do the companies with a more diversified business base. This is particularly the case if the contract is for a large system, or if there will be few opportunities to bid for similar work.

UNMANNED DRONE AIRCRAFT

Senator THURMOND. According to recent newspaper reports, one area of investigation by the U.S. attorney involves unmanned drone aircraft. It is alleged there was a non-competition in the Navy for a drone air vehicle developed in Israel. Can GAO determine if and how our procurement rules were applied in this case?

Mr. BOWSHER. The drone in question is the Navy's PIONEER Unmanned Aerial Vehicle (UAV) purchased through the AAI Corporation of Baltimore, Maryland and produced by Mazlat, Ltd., an Israeli firm. The current investigation by the Departments of Justice and Defense includes the procurement of this system. Therefore, we have no plans to investigate this matter.

Senator THURMOND. There are at least two other companies capable of performing this mission for the Navy. In fact, I wrote the Secretary of Defense last year urging that the Department of Defense insist upon competition in procurement for these drones. There is considerable money in past and present defense bills being spent by the Navy in this area. Why should this program be allowed to continue?

Mr. BOWSHER. In our recent briefings to the staffs of the Senate Appropriations Committee and the House Armed Services Committee, we have questioned the Navy's need to continue to support the PIONEER system with limited participation by the Army and none by the Air Force. The PIONEER is a system that apparently will not meet DOD's requirement for a short range common-service UAV. The Navy currently has five PIONEER systems and is contracting for four additional systems. The Navy plans no further procurement of full pioneer systems after fiscal year 1988.

Senator **Thurmond**. If GAO finds these allegations are well founded, should it not follow that real competition be held? Certainly we should not continue to fund a program that was nurtured and promoted with government money at the expense of U.S. competitors who were eliminated unfairly?

Mr. **Bowsher**. The DOD Joint UAV Master Plan calls for competing a short-range joint-service system in the early 1900s. DOD officials say they have no intentions to continue development and acquisition of the PIONEER, except as required for near-term testing and for maintaining a limited operational capability until the joint-service system is fielded. However, the requirement for the joint-service system has to be defined by the Joint Requirements Oversight Council which will not occur until sometime in 1990.

Senator **Thurmond**. Has GAO determined if there are other drone programs besides the one mentioned in the press in which the Navy closed off real competition?

Mr. **Bowsher**. The Navy is currently testing another long-range UAV called the AMBER which was developed on a noncompetitive basis by the Defense Advanced Research Projects Agency. Ten of the air vehicles were purchased for development of operational concepts. According to the DOD Joint UAV Master Plan, there is no production planned for the AMBER, unless it is required for the DOD Joint UAV Program.

[Whereupon, at 4:33 p.m., the committee was adjourned.]

DEFENSE ACQUISITION PROCESS

TUESDAY, JULY 12, 1988

U.S. SENATE,
COMMITTEE ON ARMED SERVICES,
Washington, DC.

The committee met, pursuant to notice, at 9:45 a.m., in room SR-325, Russell Senate Office Building, Senator Sam Nunn (chairman) presiding.

Present: Senators Nunn, Exon, Levin, Kennedy, Bingaman, Dixon, Wirth, Shelby, Warner, Cohen, Quayle, Wilson, Gramm, and McCain.

Staff present: Arnold L. Punaro, staff director; Carl M. Smith, staff director for the minority; Romie L. Brownlee, deputy staff director for the minority; Patrick A. Tucker, minority counsel; Andrew S. Effron, counsel; Gerald K. Bankus, Robert E. Bayer, Jonathan L. Etherton, Judith A. Freedman, Sherri Wasserman Goodman, John J. Hamre, George K. Johnson, Jr., James R. Locher III, professional staff members; Barbara L. Braucht, Mary J. Kampo, Cindy Pearson, and Pamela G. Powell, staff assistants.

Also present: Jeffrey B. Subko, assistant to Senator Exon; Gregory J. Weaver, assistant to Senator Levin; Linda Gustitus, assistant to Senator Levin; Peter K. Levine, assistant to Senator Levin; William J. Lynn, assistant to Senator Kennedy; Edward M. McGaffigan, Jr., assistant to Senator Bingaman; Charles C. Smith, assistant to Senator Dixon; Milton D. Beach, assistant to Senator Glenn; Leon Fuerth, assistant to Senator Gore; Robert K. Griffith, assistant to Senator Wirth; Terrence M. Lynch, assistant to Senator Shelby; Mark J. Albrecht, assistant to Senator Wilson; and Anthony H. Cordesman, assistant to Senator McCain.

OPENING STATEMENT OF SENATOR SAM NUNN, CHAIRMAN

Chairman NUNN. The meeting will come to order. This morning the committee conducts its second in a series of hearings on the Defense Acquisition System.

Yesterday, the Comptroller General of the United States, Mr. Charles A. Bowsher, provided us with an overview of the problems with the acquisition system. Mr. Bowsher, an independent officer who served as a senior Pentagon official under both Presidents Johnson and Nixon, made it clear that the defense acquisition system is plagued by serious management deficiencies.

I want to state again here today what I said at the outset of the hearings yesterday, and that is that it is very important to place the current allegations of fraud within the context of other problems within the acquisition system, and not simply look at the question of fraud, as serious as it is, because fraud is not the only problem, and indeed it may not be the most serious problem, in terms of the overall dollars involved.

Our committee has been particularly concerned over the years at the inability of the acquisition system to provide our men and women in uniform with quality equipment on a timely and cost-effective basis. We have been concerned about the delay, for instance, in the developing armor and anti-armor capability. We have an example of the Soviet Union having dramatically eroded the capability of NATO's anti-tank weapons by installing reactive armor on its tanks. Although reactive armor was invented in the United States nearly 18 years ago, the Army ignored this capability until quite recently.

We have other problems that do not relate to fraud. The average military production line in this country is running at less than half of production capacity. Billions are wasted on excess overhead because we rarely buy weapons systems at the production rate forecast at the outset of the program.

I know Secretary Carlucci is very familiar with this problem and tried to take the cuts this year in a way to avoid that problem becoming worse. The average major acquisition program is 3 years behind schedule and production. That does not count the 12 to 15 years it takes to develop a new weapon.

We spend billions of dollars on developing new capabilities, but many times we dissipate that investment by a lengthy development process, followed by stretching out the production lines. When I say we, I mean all of us, including the Congress, because we are all involved in that stretching out process, which is always tempting, but usually very, very costly.

Some observers have described the current scandal as an isolated problem involving a few bad apples. I think though, we have a more significant problem, a broader problem. We will be getting into that today.

I think we will certainly be asking the Secretary of Defense about a lot of different processes and procedures that he is instigating now, changes that he plans to make; we will, as I have said before, stay away from the investigative aspects of this case.

I do not think the Secretary is part of the investigative process at this stage, but even if he has information, we do not want to in any way interfere with the ongoing criminal investigations.

Mr. Secretary, we are delighted to have you and Dr. Costello and Ms. Buck here this morning. Senator Warner, do you have any opening remarks?

Senator **Warner**. Very briefly, Mr. Chairman. As I join you, we have tried to structure this hearing and all work that we perform, in the context of the investigation on procurement so as not, in any way, to infringe or jeopardize the ongoing work of the Department of Justice.

I think the basic formula that we should follow, Mr. Chairman, is we wait until the facts are in before we rush to judgment, either in terms of what may be needed to revise the procurement process, or such additional law as it might be required to deter people from committing like acts, as are alleged in this case.

And last, we must bear in mind that as we are sitting here this morning, looking into this subject, 99.999 percent of the people involved in the procurement process are going about their duties as they have in the past, today, and tomorrow, in an honest and straightforward fashion, both within government and within the private sector. And we must do everything we can to protect them so that they can carry on the work that is essential to our national defense.

Chairman NUNN. Mr. Secretary, we're pleased to have you this morning.

Senator WARNER. Mr. Chairman, I understand that one of our colleagues here is very anxious to make an opening statement.

Chairman NUNN. Senator McCain.

Senator McCAIN. Thank you, Mr. Chairman. I will be brief. I appreciate the opportunity to make a statement here, and I want to emphasize the respect and admiration we have for Secretary Carlucci and the outstanding job he has done in the past and that he is now doing in attacking this very serious issue.

I think it is easy to talk about reforming defense procurement. I think we need to recognize that requiring more paperwork, more coordination, and more delay may simply increase cost and inefficiency, and not force more honesty on the system.

In fact, the current system is already extremely cumbersome and filled with redtape that may well make it easier for those willing to violate the law to hide their activities.

I am not sure, Mr. Chairman, that we need more laws and regulations as much as we need to enforce the ones we already have. I have several points I would like to make that I think that we need to pursue.

First, we need to continue the way the Reagan administration has already proceeded: encourage the FBI and Defense Investigative Service to do their job.

Second, increase the resources available for investigation and prosecution. Too often we lack the resources to investigate indications of corruption and then conclusively prove guilt all the way through an actual trial.

Third, announce a zero tolerance policy. Announce an end to all plea bargaining and acceptance of anything less than the most severe financial penalty, and make it clear we will prosecute an appeal to the end, and seek the maximum jail sentences and fines.

Fourth, hold companies and their senior management accountable for policing their own activities and enforcing punishments. The solution to this particular problem is to hold the head of a division or corporation president responsible for any action affecting his or her company. We need penalties that, at a minimum, wipe out a convicted company's profits for at least a year.

Fifth, establish whistleblower rewards based on a percentage of the value of the crime, and force the company involved to pay for them.

Sixth, hold managers and officials in military service and the Department of Defense accountable for what happens on their watch.

And seventh, eliminate the conflicts of interest in the Congress that may be as damaging as any form of corruption within the executive branch.

If some of these measures seem Draconian, I think it is worth pointing out that many people within the Department of Defense and many senior defense contractors feel the same way that I do. There is no shortage of honest men and women in our defense industries and in the Department of Defense, and as a supporter of strong defense posture, I also see no other choice.

The American people clearly are not going to support the funding we need to maintain our defense commitments and sustain an effective defense posture unless they believe in the integrity of our defense establishment and believe the guilty will really be punished.

I look forward, Mr. Secretary, to working with you, as I know this entire committee does, and I am reminded of the words of Chairman Mao, who said it is always darkest before it is totally black. Thank you, Mr. Chairman.

[The prepared statement of Senator John McCain follows:]

PREPARED STATEMENT BY SENATOR JOHN MCCAIN

The ongoing investigation of defense contractor fraud has been dubbed "Pentagate", although the facts surrounding this fraud are still far from clear. There is no doubt that this investigation deals with very serious problems, but we should keep two things in mind. First, the vast majority of men and women involved in defense procurement and defense industry are honest and are dedicated to helping this Nation develop an effective defense. Second, fraud does exist, in spite of this administration's expanded and diligent efforts to eliminate it, and the public disgust with such fraud and waste is the most serious single factor undermining public support for a strong defense.

Politics is an arena where is always tempting to rush to judgment—particularly in an election year. It is equally tempting to hold hearings, form a commission, or pass new laws. Although these steps are sometimes helpful, their main impact is to grasp the headlines and defer the issue. Hearings and commissions don't solve problems, they merely publicize them. Worse, this approach almost inevitably leads to new laws and regulations whose main effect is to harass the innocent when the goal should be to punish the guilty.

It is easy to talk about reforming defense procurement. We need to recognize, however, that requiring more paperwork, more coordination, and more delay will probably simply increase cost and inefficiency, not force more honesty on the system. In fact, the current system is already so cumbersome and filled with red tape that it may well make it easier for those willing to violate the law to hide their activities.

We do not need more laws and regulations as much as we need to enforce the ones we already have. We spend remarkably little time actually sending anyone to jail. In my view, sending the guilty to jail has become absolutely critical to both discourage further scandals and promote the confidence of the American people in our defense programs. Time and again, the only punishment for a defense scandal is a plea bargain, a minor corporate shake-up, punishment for some low level consultant, or endless litigation followed by a payment that has little impact on a major defense contractor.

We need to change this state of affairs, and we need to change it quickly. The administration should announce now—before the specifics of the ongoing investigation are made public—a new law enforcement policy for defense contractors. We can do this with a seven point program that focuses on punishing the guilty, rather than harassing the innocent:

First, we need to continue in the way the Reagan administration has already proceeded: Encourage the FBI and the Defense Investigation Service to do their job without any interference or appearance of interference.

Second, increase the resources available for investigation and prosecution. Too often, we lack the resources to investigate indications of corruption, and then conclusively prove guilt all the way through on actual trial.

Third, announce a "zero tolerance" policy: Announce an end to all plea bargaining and acceptance of anything less than the most severe financial penalty and make it clear we will prosecute and appeal to the end and seek the maximum jail sentences and fines.

Fourth, hold companies and their senior management accountable for policing their own activities, and to enforce punishments that will deter management from tolerating any criminal or corrupt action. We need to treat corrupt defense contractors like a member of organized crime or a major drug peddler. The rewards are so great that many low level executives and consultants can always be found to operate as potential scapegoats while senior executives, and the corporation, go free or escape with penalties that do not equal the profit from violating the law.

The solution to this particular problem is to hold the head of division or corporation president responsible for any action affecting his or her company, and in many cases the Chairman of the Board. We also need to make firm use of debarment to make it clear that top company officials get no second chance. If a company is convicted of defrauding the government, it should be debarred from further contracts until the top officials of the company are removed forever, and without a dime by way of golden handshakes.

At the same time, we need to firmly attack the company profit margin or bottom line. Fines are meaningless if the overall result of bribery, spying, and influence peddling is higher overall profit. We need penalties that at a minimum wipe out a convicted company's profit for at least a year.

The penalty should be especially stiff in a case where a company illegally wins a contract. At present, it is difficult to recompete many contracts because of the risk of delay to a vital national security program. This would not be the case if a guilty company lost all technical rights, tooling, and other equipment the government has paid for, since another company could rapidly take up the slack in production. It may, however, require new legislation requiring a convicted company to divest all scandal related R&D and production facilities.

Fifth, establish "whistleblower" rewards based on a percentage of the value of the crime and force the company involved to pay for them. While many companies may be able to afford vast legal fees, few can defend themselves from "whistleblowers" within. We can discourage false alarms by making the rewards contingent on the outcome of prosecution or a financial settlement.

Sixth, hold managers and officials in military services and the Department of Defense accountable for what happens on their watch. We cannot exempt the military services and/or defense agencies from responsibility. We should freeze promotions for all senior officers and civilians associated with any program where there is corruption, or which significantly fails to deliver results with the promised cost and effectiveness and at the promised time. The time has come when every military officer and defense official directly responsible for preventing fraud and abuse has to know that the issue that will shape their professional future isn't criminal guilt, it is whether they allow serious mismanagement to occur in any form.

Seventh, eliminate the conflicts of interest within the Congress that may be as damaging as any form of corruption within the Executive Branch. Make any speaking fees and transportation payments to members of the Congress and their staffs from defense contractors illegal. Apply the same limits on hiring Congressional staff that are applied to military and civilian personnel in the Department of Defense. This would still allow the Congress to serve constituent interests, but would establish a consistent standard of ethical behavior throughout the U.S. government.

If some of the measures and punishments in this seven point program seem Draconian, it is worth pointing out that many people within the Department of Defense, and many senior defense contractors, feel the same way that I do. There is no shortage of honest men and women in our defense industries and in the Department of Defense. There is no shortage of honest defense contractors and demanding defense managers that will not tolerate even the hint of corruption. Anyone else, and indeed any firm, is expendable.

As a supporter of a strong American defense posture, I also see no other choice. The American people aren't going to support the funding we need to maintain our defense commitments and sustain an effective defense posture unless they believe in the integrity of our defense establishment, and believe the guilty will really be punished. Further, every company working in defense and every employee, and every military officer and civilian official involved in defense procurement, will suffer for the actions of the few. The time has come to punish those few and drive them out of the system.

I will do everything possible during the coming hearings on the defense scandal, and the efforts of the Senate to deal with this scandal, to put these ideas into law.

Chairman Nunn. Thank you, Senator McCain. Senator Exon.

Senator **Exon**. Thank you, Mr. Chairman. I will be extremely brief.

I just want to say, Mr. Carlucci, that we are delighted to have you here this morning. This looks like we have a serious problem on our hands. I know that you are going to do everything that you can to get to the bottom of that.

My major concern over and above getting the defense procurement matter straightened out is a concern that I have for the long-range adverse effect that this might have on our national defense as a whole.

But I congratulate you for the steps that you have taken, sending a signal that you will not hesitate in canceling contracts. When you say that, I know that you recognize, as I think most of us do, that canceling some of our black programs could have an extremely adverse effect on our national defense. I think that has to be an overall worry.

I simply want to say that, as one Senator, I have the utmost respect for you, your integrity, and I think we have got the right person in the right place at the right time to begin to get this straightened out.

Chairman **Nunn**. Thank you, Senator Exon.

Mr. Secretary.

STATEMENT OF HON. FRANK C. CARLUCCI, SECRETARY OF DEFENSE, ACCOMPANIED BY ROBERT B. COSTELLO, UNDER SECRETARY OF DEFENSE FOR ACQUISITION, AND KATHLEEN BUCK, GENERAL COUNSEL

Secretary **Carlucci**. Thank you very much, Mr. Chairman, members of the committee. I have a prepared statement. With your permission I would submit it for the record and make some abbreviated comments.

Mr. Chairman, I welcome this opportunity to appear before the committee to discuss our Nation's defense acquisition system. This committee's strong interest in the state of that system reflects the concern of all Americans that we provide our Armed Forces with top quality weapons as effectively and efficiently as possible.

The Justice Department's ongoing military procurement investigation understandably raises questions about the health of that system. In this hearing today we will not be able to come up with a definitive diagnosis of the system, especially since none of us yet knows what the Justice investigation will uncover.

But even if the probe reveals no more than the misdeeds of a few greedy law breakers, I would still like to move forward now in cooperation with the Congress, to remedy flaws in our system, regardless of whether those flaws are related to the Justice Department investigation.

In my judgment, there are defects in how America equips its forces. Some can be traced to DOD, some to Congress, and some to industry. And some have simply not been adequately addressed by any of us. But our challenge is not to assign blame. Our challenge is to get to work with a bipartisan comprehensive effort.

Before we get into specific issues, let me highlight several guideposts that I believe we should analyze in developing possible procurement reforms.

Guidepost No. 1. Reforms should target causes, not symptoms. As we consider how to remedy problems with our procurement system, we should look beyond just tightening laws, increasing enforcement, and other treatments of symptoms. To prevent violations, yes, we must detect and punish them aggressively. But we must also scrutinize the procurement system for possible causes of such wrongdoing.

Targeting causes, not symptoms, means being suspicious of hasty or piecemeal reforms which would do more harm than good. It also means being comprehensive in our scrutiny. To confine reform to the Pentagon, for example, would be to ignore what I believe are fundamental flaws beyond Defense Department control.

To illustrate the need for comprehensive reform, I would note that one major cause of procurement waste and possibly fraud is instability. Instability in individual military programs, and instability in the overall defense budget.

When funding beyond the current fiscal year is always uncertain, planning and long-term investment make little sense. Short term political intervention does. Reducing instability clearly requires a comprehensive effort, and must include the Congress.

Year in and year out, DOD tries to minimize the effects of instability, but that is no substitute for a fundamental fix.

My second guidepost is I know, of concern to this committee, and that is that reform should build on progress to date. Contrary to the assertions of some, our Nation has, in this decade, markedly improved its defense acquisition system, with the initiatives beginning in 1981 and continuing through the implementation of the Packard Committee recommendations.

The Justice Department probe should, in no way, tarnish the progress DOD and the Congress have made to date. Our DOD acquisition system still needs some more time to absorb and adjust to the past reforms. Still, that reality need not preclude carefully crafted changes. It does mean that we must be cautious and judge how difficult our proposals would be to implement.

My third guidepost is that reform should simplify, not complicate defense procurement. Defense acquisition is already too complex. Adding more provisions and prohibitions could be counterproductive, especially if underlying causes go untreated.

No amount of rulemaking can eliminate rulebreaking. Unnecessary complexity wastes time, money, and energy. Effective reform must strike a balance between trade-offs that we encounter with acquisition issues.

For example, there must be a balance between controls on the one hand and flexibility on the other. If we severely limit the ability of DOD acquisition decisionmakers to apply their subjective judgment for fear it can be improperly influenced, we then face a trade-off of allowing them too little flexibility to make the best decision.

Guidepost four is, reforms should strengthen America's defense industrial base. This could be the most important guidepost we should consider. If the consequence of a reform is to discourage firms from seeking defense contracts, then we are moving backwards, not forward.

Ill-conceived reforms can quickly convince many firms that defense business does not provide a sufficient chance for reasonable profit to make it worthwhile, or to compensate for the perennial stops and starts of military business. P/E ratios in the industry are already low. If we drive them down further, the industry will lack the capital to keep up with modernization.

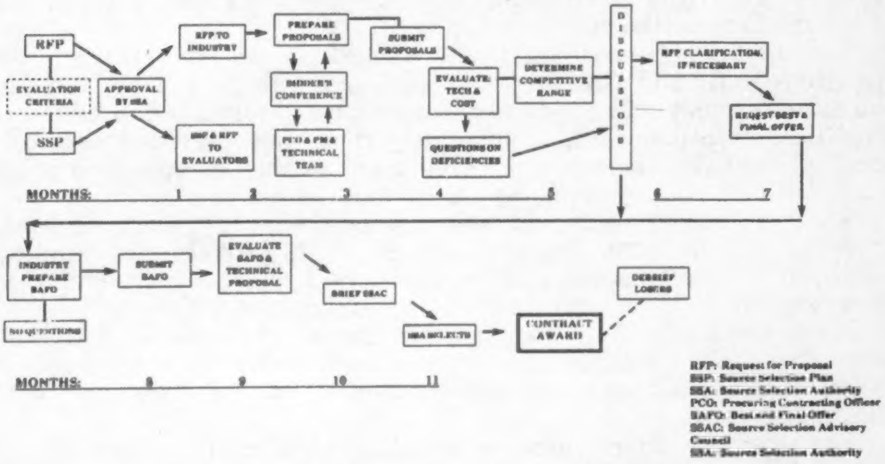
Guidepost five, reform must keep users involved in acquisition. A remedy for procurement difficulties is not to exclude from the process the military professionals who will use the defense systems we buy. Our military people have a vital interest in the quality of those systems and in how effectively we buy them.

We must retain user involvement in defense acquisition. That means the military services must continue to play a major role. It means being suspicious of proposals that would further separate acquisition responsibilities from military users by taking away major functions currently under the services and centralizing them under Secretary of Defense for Acquisition.

The authority for key acquisition decisions should not be separated from the basic responsibility and accountability for program execution.

Mr. Chairman, I want to wrap up my opening statement by showing you a chart or perhaps a couple of charts that highlight what I see as a central flaw in defense acquisition. This is a plethora of what I refer to in my full statement as intervention points.

SOURCE SELECTION EVENTS


RFP
EVALUATION CRITERIA
SSP
APPROVAL BY SSA
RFP TO INDUSTRY
SSP & RFP TO EVALUATORS
PREPARE PROPOSALS
BIDDER'S CONFERENCE
PCO & PM & TECHNICAL TEAM
SUBMIT PROPOSALS
EVALUATE: TECH & COST
QUESTIONS ON DEFICIENCIES
DETERMINE COMPETITIVE RANGE
DISCUSSIONS
RFP CLARIFICATION, IF NECESSARY
REQUEST BEST & FINAL OFFER
MONTHS: 1 2 3 4 5 6 7
INDUSTRY PREPARE BAFO
NEGOTIATIONS
SUBMIT BAFO
EVALUATE BAFO & TECHNICAL PROPOSAL
BRIEF SSAC
SSA SELECTS
CONTRACT AWARD
DEBRIEF LOSERS
MONTHS: 8 9 10 11
RFP: Request for Proposal
SSP: Source Selection Plan
SSA: Source Selection Authority
PCO: Procuring Contracting Officer
BAFO: Best and Final Offer
SSAC: Source Selection Advisory Council
SSA: Source Selection Authority

This first chart shows you the number of steps that we must go through to get a program on line. If you look at that chart, you will see that there are approximately 24 steps there. And maybe that is not bad. Except that up in the upper lefthand side, in the middle tier, you see that we have a number of other committees that are also involved in the process.

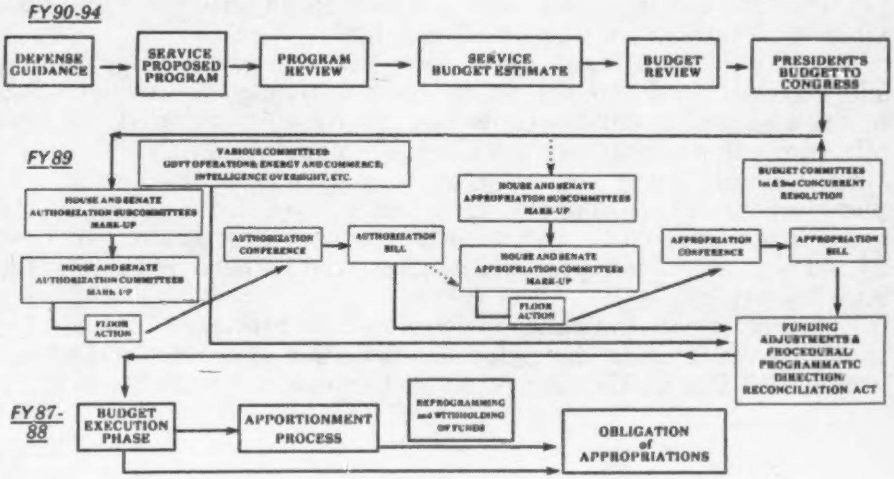
But I would agree that we need a thorough process here in the Congress to look at our programs. The problem is that when you get down to this point, you start all over again with your program. Unless, of course, it is an aircraft carrier.

But, say you are a program officer and you are developing missile systems. And you get them through that cycle down to that point, and just about the time you are implementing it, another bill comes along and there are changes in your program.

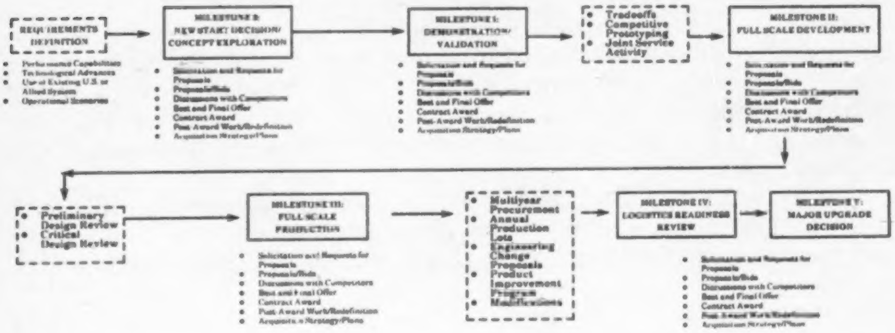
So there is no way you can plan on a sensible basis. You have to plan for change. If you are a contractor, you are looking at the other side of the coin. And once that cycle starts again, you have 24 more intervention points, 24 more points where you can influence the process.

But that is just the start. We have other processes that overlay that process. This is the defense acquisition process, the Defense Acquisition Board. This is how we go through our milestones.

CRITICAL REVIEW POINTS IN THE DOD BUDGETING AND LEGISLATIVE OVERSIGHT PROCESSES


FY 90-94
DEFENSE GUIDANCE
SERVICE PROPOSED PROGRAM
PROGRAM REVIEW
SERVICE BUDGET ESTIMATE
BUDGET REVIEW
PRESIDENT'S BUDGET TO CONGRESS
FY 89
VARIOUS COMMITTEES: GOVT OPERATIONS; ENERGY AND COMMERCE; INTELLIGENCE OVERSIGHT, ETC.
BUDGET COMMITTEES 1st & 2nd CONCURRENT RESOLUTION
HOUSE AND SENATE AUTHORIZATION SUBCOMMITTEES MARK-UP
HOUSE AND SENATE AUTHORIZATION COMMITTEES MARK-UP
FLOOR ACTION
AUTHORIZATION CONFERENCE
AUTHORIZATION BILL
HOUSE AND SENATE APPROPRIATION SUBCOMMITTEES MARK-UP
HOUSE AND SENATE APPROPRIATION COMMITTEES MARK-UP
FLOOR ACTION
APPROPRIATION CONFERENCE
APPROPRIATION BILL
FUNDING ADJUSTMENTS & PROCEDURAL/ PROGRAMMATIC DIRECTION/ RECONCILIATION ACT
FY 87-88
BUDGET EXECUTION PHASE
APPORTIONMENT PROCESS
REPROGRAMMING and WITHHOLDING OF FUNDS
OBLIGATION of APPROPRIATIONS

CRITICAL REVIEW POINTS IN THE DEFENSE ACQUISITION PROCESS (10-25 YEARS)


REQUIREMENTS DEFINITION
Performance Capabilities
Technological Advances
Use of Existing U.S. or Allied Systems
Operational Scenarios
MILESTONE 0: NEW START DECISION/ CONCEPT EXPLORATION
Solicitation and Requests for Proposals
Proposals/Bids
Discussions with Competitors
Best and Final Offer
Contract Award
Post-Award Work/Redefinition
Acquisition Strategy/Plans
MILESTONE I: DEMONSTRATION/ VALIDATION
Solicitation and Requests for Proposals
Proposals/Bids
Discussions with Competitors
Best and Final Offer
Contract Award
Post-Award Work/Redefinition
Acquisition Strategy/Plans
Tradeoffs
Competitive Prototyping
Joint Service Activity
MILESTONE II: FULL SCALE DEVELOPMENT
Solicitation and Requests for Proposals
Proposals/Bids
Discussions with Competitors
Best and Final Offer
Contract Award
Post-Award Work/Redefinition
Acquisition Strategy/Plans
Preliminary Design Review
Critical Design Review
MILESTONE III: FULL SCALE PRODUCTION
Solicitation and Requests for Proposals
Proposals/Bids
Discussions with Competitors
Best and Final Offer
Contract Award
Post-Award Work/Redefinition
Acquisition Strategy/Plans
Multiyear Procurement
Annual Production Lots
Engineering Change Proposals
Product Improvement Program
Modifications
MILESTONE IV: LOGISTICS READINESS REVIEW
Solicitation and Requests for Proposals
Proposals/Bids
Discussions with Competitors
Best and Final Offer
Contract Award
Post-Award Work/Redefinition
Acquisition Strategy/Plans
MILESTONE V: MAJOR UPGRADE DECISION

Milestone Zero, new start, concept exploration to demonstration validation to full-scale development to full-scale production. Generally, and this does not apply to every program, with each step in that process, you go through the process of letting contracts.

They too, are intervention points. The contractor sees them as targets of opportunity and, quite commonly, we get instructions, either in report language or in statute, directing us that we ought to have competiton in this program or sole-source in that program or dual-sourcing. So, once more, another point of intervention for the contractor.

Finally, we have the actual source selection process itself, which is really complex, where we go generally to best and final offer, and there are opportunities for the contractor to intervene in that process.

So we go through a series of steps here, where the process can be influenced. And if you will bear in mind, that, in a given program, that process is repeated multiple times, the opportunities for political intervention are great.

So let me just repeat what I said earlier. If you are a defense contractor, and looking at how you would make your investment, and you look at the instability in these programs, as you look at that process, and your choice is making your investment in long-term productivity enhancing equipment to try to get unit costs down and improve quality, or intervening the political process at any one of these points, either in DOD or in the Congress, you are most likely to come to the conclusion that political intervention is the best use of your resources.

So we have provided the wrong series of incentives by having so many intervention points in the system. In closing, Mr. Chairman, let me again stress my determination to work in cooperation with the Congress toward improving defense acquisition. The challenge is complicated and frustrating.

In this hearing, we are not likely to settle on definitive answers to questions we all have about how to be better at equipping our Armed Forces. But I am confident that we can move forward together and use this Justice Department investigation as a stimulus for strengthening our defense acquisition system and, thereby, ensuring our Nation's security in the years ahead. Thank you very much, Mr. Chairman.

[The prepared statement of Secretary Carlucci follows:]

PREPARED STATEMENT BY SECRETARY OF DEFENSE FRANK C. CARLUCCI

Mr. Chairman, I welcome this opportunity to appear before this committee to discuss our Nation's defense acquisition system. This committee's strong interest in the state of that system reflects the concern of all Americans that we provide our Armed Forces with top quality weapons as efficiently as possible.

The Justice Department's ongoing military procurement investigation understandably raises questions about the health of our defense acquisition system. In this hearing today, we will not be able to come up with a definitive diagnosis of that system, especially since none of us yet knows what the Justice investigation will uncover. But even if the probe reveals no more than the misdeeds of a few greedy lawbreakers, I still want to move forward now, in cooperation with Congress, to remedy flaws in our system, regardless of whether those flaws are related to the Justice investigation.

In my judgment, there are defects in how America equips its forces. Some can be traced to DOD, some to the Congress, some to industry, and some simply have not been adequately addressed by any of us. But our challenge now is not to assign blame. Our challenge is to get to work with a bipartisan, comprehensive effort. As you know, I already have a DOD task force scrutinizing our acquisition system and closely monitoring the Justice investigation. My staff and I look forward to working with the Congress toward our common goal of excellence and efficiency.

In our discussions here today, I would be happy to get into whatever detail you would like, but in my prepared statement I primarily want to suggest how our efforts ought to proceed and what our objective should be. In particular, I want to highlight several guideposts that I belive we should follow in analyzing possible procurement improvements.

GUIDEPOST 1: REFORM SHOULD TARGET CAUSES, NOT SYMPTOMS

As we consider how to remedy problems with our procurement system, we should look beyond just tightening laws, increasing enforcement, and other treatments of symptoms. To prevent violations, yes, we must detect and punish them aggressively. But we must also scrutunize the procurement system for possible causes of such wrongdoing. In the end we may find that greed, not the system, causes most of the misdeeds. But I believe we also can find ways in which the acquisition system could reduce the opportunities and incentives for greed to prevail.

Targeting causes, not symptoms means being suspicious of hasty or piecemeal reforms, which could do more harm than good. It also means being comprehensive in our scrutiny, to confine reform to the Pentagon, for example, would be to ignore what I believe are fundamental flaws beyond Defense Department control.

To illustrate the need for comprehensive reform, I would note that one major cause of procurement waste, and possibly fraud, is instability—instability in individual military programs and instability in the overall defense budget. When funding beyond the current fiscal year is always uncertain, planning and long-term investment make little sense. Short-term political intervention does. Reducing instability clearly requires a comprehensive effort and must include Congress. Year in and year out, DOD tries to minimize the effects of instability, but that is no substitute for a fundamental fix. A start would be biennial budgeting, which I know many on this committee support. Congressional approval of more multiyear procurement proposals also would help, and add to our $7.5 billion in savings since fiscal 1982 from that approach.

Another underlying cause of procurement problems is the number of opportunities for defense contractors to influence procurement decisions, both in the Pentagon and in Congress. Our current procurement system has too many of what I would term "intervention points"—that is opportunities for friendships or political clout to carry more weight than contractor performance or product quality and cost. We can reduce these opportunities for intervention through such techniques as long-term contracts, simplifying specifications, freezing weapons designs, contracting to performance, and multiyear approvals of programs. But I would also challenge Congress to study ways to reduce its role in this problem of political intervention in defense procurement decisions.

If we target causes not symptoms, we can change the incentives created by our acquisition system, and that is the real key to genuine reform. In many ways our system rewards precisely what we want to avoid. For example, the aforementioned problems of instability and political intervention create incentives for defense contractors to (1) concentrate on short-term profits at the expense of long-term investment; (2) divert funds and management attention to trying to intervene in congressional and DOD decisions; and (3) aggressively seek information and access affecting contract awards, through consultants or other means. Clearly we would like to change these incentives.

I know my second guidepost is a concern on this committee.

GUIDEPOST 2: REFORM SHOULD BUILD ON OUR PROGRESS TO DATE

Contrary to the assertions of some, our Nation has in this decade markedly improved its defense acquisition system, with the initiatives beginning in 1981, and continuing through implementation of Packard Commission recommendations. The Justice Department probe should in no way tarnish the progress DOD and Congress have made. Some of the wrongdoing being uncovered may simply be violations of the law, not system deficiencies. Some system flaws highlighted by the probe may be ones that our Government has not really tackled, such as budget instability and political intervention points. Some uncovered flaws perhaps were unforseeable and possibly unavoidable consequences of past reforms. For example, one of the most complex issues we face is the impact of increased competition for contracts. High-stakes competition may cause difficult problems that are just now surfacing.

This last point also suggests that our DOD acquisition system still needs more time to absorb and adjust to past reforms. Still, that reality need not preclude carefully crafted changes. It does mean we must be cautious and judge how difficult our proposals will be to implement.

My third guidepost is one I believe we all share:

GUIDEPOST 3: REFORM SHOULD SIMPLIFY, NOT COMPLICATE DEFENSE PROCUREMENT

Defense acquisition is already too complex, adding more provisions and prohibitions could be counter-productive, especially if underlying causes go untreated. No amount of rulemaking can eliminate rulebreaking, unnecessary complexity wastes time, money, and energy.

The consequences of complexity illustrate that effective reform must strike a balance between tradeoffs we encounter with acquisition issues. For example, there must be a balance between controls on the one hand and flexibility on the other. If we severly limit the ability of DOD acquisition decisionmakers to apply their subjective judgment for fear it could be improperly influenced, then we face a tradeoff of allowing them too little flexibility to make the best decision.

It does not help when critics ignore these kinds of tradeoffs. It makes little sense, for instance, to call for a "crack-down" on consultants without considering the inescapable tradeoffs, such as diminished expertise available to DOD and industry.

These tradeoffs relate to the fourth guidepost:

GUIDEPOST 4: REFORM SHOULD STRENGTHEN AMERICA'S DEFENSE INDUSTRIAL BASE

This may be the most important guidepost we should consider. If the consequence of a reform is to discourage firms from seeking defense contracts, then we are moving backwards, not forward. Ill-conceived reforms can quickly convince many firms that defense business does not provide a sufficient chance for a reasonable profit to make it worthwhile or compensate for the perennial "stops and starts" of military business. P/E ratios in the industry are already low. If we drive them down further, the industry will lack the capital to keep up with modernization.

Our goal should be to:

Promote the global competitiveness of defense firms.

Achieve depth and flexibility—to avoid, if feasible, having only one firm or one factory in key industrial areas.

Encourage long-term industry investment to increase productivity and advance new technologies.

Nurture the development of a technological skill base, so we will have the expertise to design and produce the defense systems we will need.

Of course, America's defense industrial base is as dependent on people as it is on technology and machines. Likewise, people are important to our DOD acquisition system, and the quality of people working on defense acquisition—both inside the Pentagon and in industry—is a critical variable when we consider thorny issues like the role of consultants and the so-called "revolving door." For example, as we discuss restrictions on officials leaving Government service to join the defense industry, we must consider whether such restrictions will discourage good people from joining or staying in our DOD acquisition staff.

The tradeoff for unnecessarily tight career restrictions on acquisition officials may well be quality and expertise available to our Nation's overall defense effort. Yes, we should study the adequacy and enforcement of rules governing the career movement of people between DOD and the defense industry. At the same time, we should realize that what some call the "revolving door" in fact benefits both DOD and the defense industry, and advances America's national security. DOD gains tremendously when we are able to recruit defense industry professionals. They bring to us valuable business experience and in-depth knowledge to help us be a demanding buyer of defense industry products. Industry and our Nation gain when military and civilian professionals leaving Government continue to apply their expertise to building a stronger U.S. military.

The quality of our defense acquisition work force gets little help from the current civilian personnel system. As pointed out by the Packard Commission and the Defense Science Board, problems in recruiting, retaining, and providing incentives for high quality scientific, engineering, and acquisition personnel are becoming acute. As one study recently described it, DOD is trying to design, acquire, and maintain 21st century technology while working under a restriction-oriented personnel system, which has its roots in 19th century civil service philosophy. This is why we've been working closely with the committee and the Office of Personnel Management in support of legislation that will allow us to test personnel systems that are less reliant on rigid classification distinctions and more reliant on pay flexibility that is market oriented and more closely linked to performance. Your bill, S. 2530 will give us that opportunity for 100,000 DOD employees. It is clearly a step in the right direction.

This point on professional expertise reinforces a fifth guidepost:

GUIDEPOST 5: REFORM MUST KEEP USERS INVOLVED IN ACQUISITION

A remedy for procurement difficulties is not to exclude from the process the military professionals who will use the defense systems we buy. Our military people have a vital interest in the quality of those systems and in how efficiently we buy them. We must retain user involvement in defense acquisition. That means the military services must continue to play a major role. It means being suspicious of proposals that would further separate acquisition responsibilities from the military users by taking away major functions currently under the services and centralizing them under our Under Secretary of Defense for Acquisition. The authority for key acquisition decisions should not be separated from the basic responsibility and accountability for program execution.

As we wrestle with the fundamental challenges I have highlighted, we must also deal with the specific issues and problems emerging from the Justice investigation. To give you a sense of the scope of our ongoing DOD efforts, let me highlight several actions of my DOD investigation task force. They include:

An examination of existing laws, regulations, and directives concerning: contractors' use of consultants; protection of contract information; ensuring that specifications do not intentionally favor any particular competitor; standards of conduct; and revolving door rules.

Establishment of a pre-award certification to be required of contractors whose conduct, as established through official information, warrants enhanced review. We will require these contractors to certify they have not improperly obtained source selection information or engaged in collusive bidding.

Consideration of a clause to recover profits from contractors found guilty of breaking the law in obtaining a contract award.

Preparation of a protocol to provide guidance on appropriate actions to be taken by the military services when new information (e.g., unsealing an affidavit) becomes available.

In addition, I will send a letter to the top 200 defense contractor chief executive officers urging them to ensure stringent management controls on the use of consultants and to avoid improper business practices.

In dealing with contractor wrongdoing, the Department of Defense already has general courses of action available to us under the law, as implemented in the Federal acquisition regulation. We will use these measures, in all cases, to protect the public interest. Our courses of action include:

Rescinding a contract based upon a conviction for bribery or conflict of interest.

After notice and a hearing, terminating a contract on the basis of a determination that a contractor, his agent or representative, offered or gave a gratuity to obtain a contract or favorable treatment. In addition, the statute authorizing this action also permits the assessment of exemplary damages of three to ten times the amount of the gratuity.

Fining an individual, in addition to other penalties, for making false claims or statements.

Negotiating a reduction in a contract price.

Suspending, or temporarily disqualifying a contractor; and debarring, or excluding for a specified period, a contractor from Government contracting to protect the Government's interests, upon conviction or civil judgment.

Before a contract award: Canceling the solicitation and beginning again; rejecting a bid or proposal based upon evidence that an offeror has misrepresented a contingent fee arrangement; or rejecting a bid or proposal suspected of being collusive and reporting it to the Attorney General.

Let me also bring the committee up to date on one other matter. Yesterday we announced the lifting of the suspension of payments imposed on July 1, 1988 on current contracts in the nine Navy programs identified in the affidavit unsealed by the Federal court in Dallas in connection with the Justice Department investigation. The decision to lift the suspension of payments on current contracts was the result of completion of a detailed Navy review of each affected program and contract in light of the information contained in the unsealed affidavit. This review, conducted during the past week, established that currently available official information did not indicate that any of the current contracts in the affected programs are tainted. If other official information becomes available during the course of the investigation which warrants new concern regarding these or other contracts, the Department will evaluate it and take any appropriate action.

In closing let me again stress my determination to work, in cooperation with Congress, toward improving defense acquisition. The challenge is complicated and frustrating, often, seemingly good ideas turn out to have deleterious tradeoffs. The best way for us to make progress is to achieve a balance between those tradeoffs, rather than ignore them so that our favorite reforms appear more dramatic and surefire.

I hope these opening remarks will help us proceed from a common perspective. In defense matters there never seem to be easy answers, and acquisition is no exception. But I am confident we can move forward cooperatively and use this Justice Department investigation as a stimulus for strengthening our defense acquisition system, thereby ensuring our Nation's security in the years ahead.

Chairman NUNN. Thank you, Mr. Secretary. I certainly agree with your basic premise that we have too many steps in the process, probably both in Department of Defense and in the Congress.

As you well know, this committee has tried our best to go toward a longer term, more stable program, including milestone authorizations, multi-year contracting, and 2-year authorization, which we just got started on.

The Governmental Affairs Committee has on their mark-up agenda a 2-year budget, not only for the authorizers, but also for the appropriators. So we share your general feelings on that and hope we can work together to make our process over here much more meaningful.

Before I get into questions on the subject of the day, without getting into any details on this at all, could you just tell us the time frame for the completion of the report on the investigation of the Airbus tragedy?

Secretary CARLUCCI. We anticipate that the report will take, I would judge, at least another 2 weeks. We have the tapes back here; the investigators are conducting interviews, so I would say somewhere in the 2 to 3 week timeframe.

Senator WARNER. Mr. Chairman, just a follow-up on that, as we face this year-end examination. Are we going to be compelled to divulge, piecemeal, some of the information that might otherwise be retained until the investigation is completed?

Secretary CARLUCCI. I should not think so.

Senator WARNER. I hope we would not.

Secretary CARLUCCI. We have no reason to divulge information at this point and certainly we have seen in the press how partial and inaccurate information can be extremely damaging.

For example, there is a story in today's Washington Post that talks about a second ship observing the airplane. We have no knowledge of that and we do not know where it comes from. So this kind of information can be very damaging.

I think it is best to wait until the entire report is in.

Senator WARNER. I share that belief.

Chairman NUNN. Mr. Secretary, when you face the problems you are faced with now, in terms of all these contracts that have come under suspicion, have you established a policy now as to the type of action you will take, a general framework with respect to contracts that are alleged to have been obtained by fraudulent means?

Secretary CARLUCCI. The task force, which is cochaired by the people on my left and right is developing a protocol in conjunction with the Service Acquisition Executives, while they are on the task force, which will provide a standard procedure for contracts that might be tainted.

Of course, even with that kind of protocol, you are going to have to look at each on a case by case basis. How tainted is the contract or what systems are at risk, what are the termination clauses in that contract? But I think we can standardize this as much as possible.

Chairman NUNN. Have we reached a point in defense contracting where there are only a few companies involved in the bidding and where the contract is, say, halfway down the road, where those are simply beyond cancellation in terms of the effect on our military forces?

It seems to me we have a real danger here of the same approach we have taken in cases of banking, where if you are a small bank you can fail. But if you are a big bank and affect the whole country, you cannot permit it to fail. Are we going to face some of that in the defense arena?

Secretary CARLUCCI. It is a possibility. Until the actual evidence is in, I cannot make a judgment of course. There are some very large programs that would have a significant adverse impact on our defense capability were we to cancel them.

But cancellation, of course, is not the only remedy. We have other remedies under the law. If there has been evidence of bribery or corruption, we can assess damages, we can assess fines. So there are various legal remedies that we have. Cancellation is not the only one.

Chairman NUNN. Do you need any other authority under law in order to have alternative remedies?

Let us say a big contractor, where there was very limited competition, has gotten the contract and it is alleged to have been by fraudulent means. If you cancel the contract, get a 5-year delay in getting the equipment to the field, the cost goes up tremendously. You are faced with that kind of a situation.

Do you have the authority under the law for alternatives that are equal to the severity of the violation?

Secretary CARLUCCI. We, of course, in cancelling a contract, absent a conviction, would have to follow certain due process procedures.

But I am advised by counsel, and I will let her speak for herself, that I have adequate authority to terminate or assess damages and to start up new contracts should that be necessary.

Chairman NUNN. Do you have any limitation on the fine? I mean, for a big contract a million dollar fine is nothing. What is the limitation on the fine under the law?

Ms. BUCK. Well, depending on the particular facts in the case, we have a broad range of legal remedies, both criminal and civil.

And within the confines of the criminal law you can look at, for example, at the bribery statutes where we can extract not only fines but sentencing to jail as well.

On the civil side, we also have a broad range of legal remedies, but we are going to have to look at a number of factors before we can determine what might be the appropriate action in each case.

We will look at, for example, on your cancellation issue, how far along the contract is, the level of taint involved in the contract. We will look at what the cost would be to the Government.

So there will be a broad range of factors that we will also want to look at before we make any decision in terms of our civil remedies.

In my judgment, based on the facts that I have seen, in part frankly on the press reports that we have seen, I think we have a broad range of legal remedies that we will be able to use as the broad investigation proceeds.

Chairman NUNN. Could you furnish for the record those legal remedies that are alternatives to cancellation, including the extent of the fines that you would be able under the law as it now exists to seek?

Ms. BUCK. Yes, sir. In fact, within our joint task force, we are right now preparing an analysis of all the legal remedies that we will have as the broad investigation proceeds. We have a preliminary draft on that right now. (See "Fraud Remedies", p. 112.)

Chairman NUNN. Mr. Secretary, when Congress established the position of Under Secretary of Defense for Acquisition, which was a Packard Commission recommendation in 1986, we also established the statutory position of Deputy Under Secretary for Acquisition. Yet for 2 years that post has remained unfilled.

We also have other acquisition gaps here. The Air Force is the only military department with a full-time Service Acquisition Executive. The Army and the Navy have designated their Under Secretaries to serve as acquisition executives.

The Under Secretary, of course, must also serve as the Secretary's alter ego on a wide variety of matters unrelated to acquisition. So my question is, is it possible to implement these Packard proposals without having Dr. Costello with an assistant and also without having those set up in the services uniformly?

Secretary CARLUCCI. I think it is possible to do it without setting them up uniformly in the services.

It depends a great deal on the skills of the particular individual. The people who have been nominated happen to have good skills in the procurement area in the services.

We are in the process of getting through the White House a nomination for Dr. Costello's deputy. We wanted to wait until Dr. Costello himself was confirmed before we moved forward on that.

Chairman NUNN. But why would it take 2 years to fill that post? When the President endorsed the Packard Commission recommendations, the Congress passed the enabling statutes, and it seems that if the system is going to work you have to carry through.

Secretary CARLUCCI. Well, because the previous incumbent resigned amid a certain amount of controversy, to be quite candid with you.

When I came in I nominated Dr. Costello. He had to go through the White House process, through the confirmation process. Once he went through that process, then he felt confident that he could pick a deputy, and that deputy is now in the personnel system.

Chairman **Nunn**. Dr. Costello, yesterday the General Accounting Office testified that your predecessor, Mr. Godwin, did not have the authority that was envisioned under the Packard Commission recommendation nor under the statute.

The testimony from Mr. Bowsher was that basically you had been undermined, at least your predecessor Mr. Godwin had, and he had seen nothing to change that, that you still did not have the authority and did not have the backing to carry out your function. Would you comment?

Dr. **Costello**. I think the Secretary has already made one of the comments that deals with personalities.

Dick Godwin did an outstanding job, as I have testified before this committee earlier, in setting up this structure. But in dealing with a large bureaucracy you have to develop a concept of consensus management. We have done that.

I have all the backing from the Secretary and from the Deputy Secretary that I think the Packard Commission ever envisioned.

In fact, we are going to be pleased to have Mr. Packard with us on Thursday with all of the program executive officers to discuss our system and how we improve it, looking at it from the perspective of Mr. Packard, looking at it from the perspective of the program executive officers from all the services; all of us meeting together to further strengthen it. This is the first time a meeting of this type has occurred. I do not see any area in which I have not had adequate authority to accomplish the job that I have been assigned.

Secretary **Carlucci**. Mr. Chairman, may I make a comment? Because this gets to an issue which has been debated, and I think is germane to the bill that Senator Dixon has introduced, and it is the question of whether the Under Secretary for Acquisition should be in charge of process and policy with authority in these areas over the individual services, or whether he should actually get into contract implementation.

It was a view with the Packard Commission and it is my view that he ought to have a very strong policy rule, and he ought to oversee the process from beginning to end and the services have to be responsive to it. And the statute makes it clear that he has authority over the services.

But he should not be dealing with 56,000 contract actions a day. That just is not feasible, the system will not work. As I said in my prepared statement, you also need to keep implementation fairly close to the uniformed services. The user has to have an input into the implementation process.

So to simply yank it up from the services and put it under the Under Secretary for Acquisition would not work. But it is my understanding, although I was not in the Pentagon at the time, that the latter approach was the approach that Mr. Godwin favored.

Chairman **Nunn**. Senator Warner.

Senator **Warner**. Mr. Secretary, you have come to the Office of Secretary of Defense with broad experience, having served as the deputy there, served on the Packard Commission, served in industry. And this morning you outline a series of what you term "guideposts" and reforms.

My first question is, where has this been? Why have we waited to see this until after this case has sprung on us rather unexpectedly? Had you intended to implement some of the reforms despite this case?

It looks as if we are reacting to the case when in fact we should have been addressing this all along.

Secretary **Carlucci**. Thank you, Senator Warner. You will note that one of the guideposts is, build on previous reforms. I make precisely that point, that we have made a lot of changes in the procurement system.

What I am seeking to do, to be quite candid with you, is to avail myself of an opportunity here to make some changes that I have long felt need to be made to make the system more productive. This offers me an opportunity to describe this in more graphic terms.

What I am telling you is nothing new. You have heard me say a number of these things to this committee before. I am describing it in somewhat different terms. I am describing it so that you can see it from the viewpoint of both the program officer, program manager, and the contractor, and you can see the kind of incentives that we create.

There will be some new things that will come out of this investigation. For example, I think we may well want to talk to you about a statute to tighten up on the use of proprietary information.

Senator **Warner**. That was my second question. What about the guidelines that exist today? And what is necessary to tighten up that situation?

Secretary **Carlucci**. I think you have to take into account that any process that deals with $165 billion in procurement has to be a dynamic process. When we detect flaws in that process, we have to be prepared to change them.

I am not saying the process is perfect at this point. Indeed, I think there are some fundamental aspects of the process that need to be looked at. On the other hand, what I am saying is, do not take all the previous reforms and throw them out, let us build on them, and let us build in a constructive way.

Senator **Warner**. Could you give us any insight into the direction that you might go on the question of proprietary information?

Because as we sit here today, people are relying on the existing regulations and procedures, and it seems to me in fairness we should give them the opportunity to know what is in our mind.

Secretary **Carlucci**. I am not a lawyer, but my understanding is that the law makes it an offense to give out proprietary data in return for some kind of compensation or remuneration. It might be wise to move to just make it an offense to give out proprietary data. But I defer to counsel.

Senator **Warner**. How about Ms. Buck?

Ms. **Buck**. Yes, I have explored some ideas concerning the protections currently in the law on proprietary data with the U.S. Attorney General.

I think that we both believe that there are some problems perhaps, at least on the criminal side, where there is an exchange of money. But we want an opportunity to discuss those ideas within our respective departments and would welcome an opportunity to come back and talk to you about that.

Senator WARNER. It appears in this area there may be grounds for additional legislation.

Ms. BUCK. My initial view is that, yes sir, that is correct. I would say that there are currently laws on the books that do address the overall subject of the handling of proprietary data.

Certainly we have specific provisions, with our own procurement regulations that address that.

Senator WARNER. Let me switch to a different subject, Ms. Buck. And that is the question of ethics.

Now, the industry—I think 46 have signed up on the voluntary basis—and I ask the Secretary and yourself, is part of the reform that you might be considering a regulation requiring the industry in its proposals to indicate that it has done its very best to try to instill in this organization a code of ethics?

Ms. BUCK. I think you are referring to our self-governance program, where we have requested various companies to, on a voluntary basis, set up an overall self-governance program. I certainly support that kind of a concept.

I am not so certain, though, that that should be something mandatory across the board for all defense contractors. That program does impose certain fairly burdensome requirements internally in a company that perhaps small businesses would have a problem coping with.

I think that we should be very careful here about making some sort of sweeping mandatory change because of the hardships that I think it could impose on small businesses who would not have in-house lawyers and a large auditing staff and would possibly have some difficulties coping with those kinds of requirements.

Senator WARNER. Is there any way we could help the small business to comply, because I certainly would want to do it as a matter of policy if they could afford it?

Ms. BUCK. Well, I think it does, especially with the tightening budgets, and I am getting into the Secretary's area here.

Senator WARNER. Perhaps the Secretary might want to address——

Ms. BUCK. I think it becomes very difficult to impose some costs on these small firms.

Senator WARNER. The general questions of ethics in the industry and how you might by virtue of regulation or otherwise require their participation.

Secretary CARLUCCI. Dr. Costello has a point.

Dr. COSTELLO. We have already established a code of ethics in the defense acquisition regulations to which we urge contractors to adhere.

Whether contractors have signed up voluntarily for this type of program will have a major impact upon their case should there be any problems in the future. So we have put it in place to say, industry, be sensitive to our concerns about ethics. And it is in the regulations already.

It has not been made mandatory for some of the reasons that Ms. Buck described.

Senator **Warner**. So you think it will probably continue on a voluntary as opposed to a mandatory basis? Or is that subject under consideration?

Secretary **Carlucci**. I am willing to look at that, Senator Warner. My general view is that these things are much more effective, human nature being what it is, if people do it in a voluntary basis, as opposed to having it imposed.

We are doing something parallel in the audit field. We have a contract risk assessment program where we go in and review a contractor's audit process. If that seems sufficiently strong, then we can ease up a bit and focus on those contractors that do not have a strong audit process.

So that we can get contractors to move themselves and a code of ethics, strengthening their audit systems, that is desirable. If we do not seem to be moving fast enough, I am willing to take a look at other measures.

Senator **Warner**. My time is up Mr. Chairman.

Chairman **Nunn**. Thank you. I believe Senator Exon is going to yield to Senator Cohen because he has another meeting to attend.

Senator **Cohen**. Thank you very much, Mr. Chairman. Secretary, welcome.

I think it is clear from your experience and ours that whenever there is a scandal there usually is a stampede to find scapegoats that probably rivals that of the running of the bulls at Paploma. And that is no different in this particular case. Congress may find itself in the way of those bulls as well.

But I would like at least to take a few moments to examine some of the charges that perhaps Congress has contributed to the complexity of our procurement system and may have opened up avenues and opportunities for the kind of fraud that is a subject, if not of this investigation, at least of major concern.

Yesterday, we had testimony from the GAO, Mr. Bowsher, and I had occasion to ask him a series of questions, because it was suggested by Mr. Bowsher that perhaps Congress had contributed to the procurement difficulties we find ourselves in today.

I asked him whether or not he believed that the Truth in Negotiating Act contributed to that, and he said no. I asked whether or not Congress, by passing the Cost Accounting Standards Board, had contributed to this deficiency that we have, he said no.

I asked about the uniform application of debarment proceedings against a contractor who is guilty of defrauding the Government, and he said no.

I asked about hurry-up spending, and another measure I am sure you are familiar with, competition in contracting. The answer was affirmative in each case, these were very positive contributions by Congress.

I then asked him about the Carlucci reforms, which you and I worked on back in 1981, as I recall, and expected him to say these have been very positive contributions. And he indicated no, the Carlucci reforms may have contributed to some of the difficulties we have now.

So I was wondering if you had occasion to talk with the GAO, because what he indicated is that part of the Carlucci reforms were to decentralize the procurement process so that you gave program managers much more flexibility and authority to deal with the contractors to eliminate some of the review processes that we have now.

And he indicated that there was a decentralization that was satisfactory, but that there was an absence or a lack of enough oversight at that level. I would like to know what your reaction to that is.

Secretary CARLUCCI. Well, I did have lunch with the Comptroller General about 2 weeks ago, and he did not raise this with me, so I am rather surprised that he raised it in testimony.

I only have to say that he is——

Senator COHEN. He raised it in response to a question, not that he was offering it.

Secretary CARLUCCI. I regret that his staff has not fully informed him about the nature of the so-called Carlucci initiatives.

Let me read you from the text of a March 27, 1981 memo that went out in parallel with the so-called 32 initiatives. The paragraph is subtitled, Decentralization and Accountability.

This memo is signed by me. I think it is signed by me. And it says, we will achieve a better defense management by working toward a system of centralized control of executive policy direction and more decentralized policy execution.

That is the policy that I have tried to follow, it is the policy that I would advocate today.

Senator COHEN. What he suggested, however, was there was an absence of enough oversight at that lower level where the discretion of decentralized program execution resides, resulting in a centralized policy with inadequate oversight. Do you have any reaction to that?

Secretary CARLUCCI. Well, my reaction to that is that in a very large organization it takes a while to change the system.

You have to put courses in place, and if I go out to the training institutes today I find courses in place that are educating the people at a lower level. And you have to have responsible people, and people who are enthusiastic about the policy. And perhaps not everybody was enthusiastic about it. But I think it is very difficult to make those kinds of generalizations.

Senator COHEN. You stated before the Philadelphia World Affairs Council earlier this month that the key to combating criminal behavior is to minimize the opportunities, monitor the system aggressively, and punish wrongdoing severely, and that is what we are doing.

One of the tools to punish wrongdoing, it would seem to me, to have a system in place for combating fraud, and in this instance Congress passed the Program Fraud Civil Remedies Act in 1986.

And it had a mechanism in it that would allow for the imposition of fines, in those program fraud cases involving under $150,000. The regulations were due to be issued in April of 1987.

NSA, GSA, most of the major procurement agencies have all issued regulations. DOD has not, as of this time, issued regulations that deal with program fraud. Could you explain to the committee why that is so?

Secretary CARLUCCI. I am informed by my general counsel that our regulations are done. We do not know if they have been published in the Federal Register, but they are coming out.

Senator COHEN. In looking at the source selection events chart, it looks quite complex, and indeed it is. But the implication is that once again we have imposed upon the Defense Department a complexity in the procurement process which is contributing to its inefficiency, to deficiencies.

What is there in the source selection process outlined on the board that you would eliminate?

Secretary CARLUCCI. I did not mean to imply that you would impose this process on us, Senator Cohen.

What I am saying is that there are innumerable points of vulnerability in the process, some of which are in the Congress, some of which are in DOD. I am currently examining that source selection process to see if there are not some points of vulnerability that can be eliminated.

One suggestion that has been made to me that Dr. Costello is examining is whether we should really go to best and final offer, whether that does not create too much pressure on the system.

I do not know. That means a little analysis. But there may well be ways that we can simplify this system, and we are looking at that.

Senator COHEN. Well, just one final point. We have been reading about the allegation concerning the B–1 bomber, the reports that it cannot carry out its mission as a penetrator because of ECM deficiencies, which at this point appear incorrectable.

What changes—first of all, are those reports true? And if so, what changes in the procurement system would you recommend to catch that kind of deficiency so we do not find we produce 100 B–1's and then discover that they cannot carry out their mission?

Secretary CARLUCCI. The reports are not accurate. The B–1 can carry out its mission. Its ability to carry out its mission is a function of a number of factors.

It is a function of its ability to fly at low levels at very high speeds, it is a function of its ability to follow the terrain, it is a function of its low radar cross-section, and it is a function of its ECM countermeasures. When all of those come together, the B–1 has a unique capability.

Now, there is clearly a weakness in ECM. But that weakness is not sufficient to say that the B–1 cannot carry out its mission. That weakness is being addressed.

Senator COHEN. What weakness in the procurement system would have caught that before the systems were actually produced and deployed, before we have a report issued that the ECM is deficient and now we have a fully completed plane which appears we cannot correct without substantial investments of dollars?

Dr. COSTELLO. I think we are looking directly at the system of program management. The program manager has to feel there is an advantage for disclosing all of the efforts, all of the rates of progress in the specifics of his program. That is buried down in the technical review of those programs.

We have put in place a defense acquisition executive system that we think will give us a better chance of monitoring those kinds of programs, the problems within a program, than has been the normal routine before.

That was a recommendation from the Packard Commission. It is up and running now. We are going through our first review. We are having detailed discussions by the technical professionals responsible for those portions of the program, saying yes, it is good, or no, we have a problem.

The OSD staff then has a responsibility for going through and describing for us a cure, what they are going to do to help that program meet all its requirements. So we have a system in place now that is an improvement over the process that was there before.

Secretary **Carlucci**. If I may add to that, Dr. Costello is putting into place what is called a total quality management initiative, where we are beginning to focus on quality in the production line instead of just quality at the end of the production line, statistical quality control measures, because what 40 percent of our defense systems cost are the logistics tail, making repairs after the system is in place. And we want to reduce that. So we are making an intensive effort.

Senator **Cohen**. Thank you, Mr. Chairman. Thank you, Senator Exon, for yielding to me.

Chairman **Nunn**. Thank you, Senator Cohen. Senator Exon.

Senator **Exon**. Thank you, Mr. Chairman.

Since we have gotten into this B–1 matter, let me just clarify for the record my view of that. That B–1 bomber has been opposed by a substantial number of individuals, and they will never let up on anything that will destroy that program.

As far as its future as a penetrator is concerned, we have on record testimony in this committee from the former Secretary of Defense that the B–1B would not be a good penetrating bomber much beyond the year 1991. Therefore, I think the B–1B is taking a bad rap in this particular matter.

I know there are problems. I know that those problems have intensified somewhat. The facts of the matter are it was an interim bomber between the B–52s and the Stealth, which should be on line, hopefully by the mid-1990's.

I would simply say that I think there are a great many things that should have the focus and attention of this and other committees of jurisdiction and oversight responsibility. But while the B–1 does not come up to what our expectations were as far as ECM is concerned, it is a very viable weapon. The 100 that we are going to buy are a very viable part of our national defense in the immediate future.

Would you agree with that statement?

Secretary **Carlucci**. I agree with it wholeheartedly, Senator Exon.

It is a very capable bomber that can penetrate. Indeed, in my own judgment it will be able to penetrate beyond 1991 and 1992.

Senator **Exon**. I want to return if I could to this matter of how we are going to prevent these things in the future. I think that deterrents, the fines that can be levied, other actions that can be taken by government officials, are going to play a key role in stopping this in the future.

As you know, there are two ways that the Government can now terminate a contract: termination by default, which is the best from the Government's standpoint as I understand it; and termination for convenience.

I am not sure that either one of those go as far as I think we should have in the law with regard to the authority exercised by the Secretary.

Is there any way, through criminal or civil penalties presently on the books, that the Secretary of Defense through proper action, maybe through the courts, could dictate that with regard to a black program—and I am talking about the big contractor now, Mr. Secretary, not the small contractors, the big contractors, that profits could be taken as a fine. As per my earlier statement, there could be a very important black program whose cancellation would seriously hurt our national security.

Is there any way that we could eliminate the profit if you had evidence that would be provable in court that improper actions had been used in the procurement process? Could you under existing law take away all the profit and make that particular corporation produce that particular vital program and take away their profit?

Secretary CARLUCCI. I think the answer to that question is yes, but let me ask counsel to go into details.

Ms. BUCK. Yes. I think that we must be very careful here to operate based on a specific set of facts. We are looking at several different alternatives along the lines of what you are discussing.

One would be a possible rescission of a contract where you have bribery involved. Another issue that we're looking at is the recoupment of profits as another measure of dealing with wrongdoing, where we have certain legal authorities to recoup profits.

And there are currently some laws on the books on those two issues.

In addition to that, we are looking in the context of our joint task force at a clause that we would be using in new awards dealing specifically with the subject of recoupment of profits.

So when I mentioned a couple of our legal remedies earlier in response to Senator Nunn's question on overall adequacy of legal remedies, I did not mean to indicate that those were the only remedies that might be available to us. I think we have a whole range of remedies, and we will be pursuing all of those, depending on the particular facts as the facts unfold in the course of the investigation.

Senator EXON. Ms. Buck, let me push you just a little further on that. Then you have remedies in addition to the termination by default or termination for convenience? Or do you think you have the latitude, either under one or both of those, to do what you just said you thought you could do?

Ms. BUCK. Yes, we are looking beyond just terminations for convenience or termination for default. Certainly, traditionally, historically within the Government, we have used both of those remedies in various contractual situations.

But as the facts unfold in the fraud investigation, we are going to look at every remedy that is available to us. And I think we will certainly look beyond terminations for convenience or terminations for default.

Senator **Exon**. Thank you.

I would just like to have you take a look at this best and final offer, Mr. Secretary. You have had a lot of experience with that. I brought this up yesterday with Mr. Bowsher, and he is going to look into it. He agreed that maybe we carry that too far sometimes and maybe we create the climate for some of the things that we are most concerned about right now.

I will have some other questions in my second round, but my time is up now, Mr. Chairman.

Chairman **Nunn**. Thank you.

We will go back to the regular order, which will be Senator Bingaman followed by Senator Quayle.

Senator **Bingaman**. Thank you, Mr. Chairman.

Mr. Secretary, first let me compliment you. I notice in your prepared statement you indicate the administration's strong support for S. 2530, which is the bill we are trying to enact this year to set up an alternative personnel system.

I agree with you, that is a step toward implementing one of the Packard Commission recommendations on which we have not made any real progress to date.

If you have any comments on that, I would be glad to hear.

Secretary **Carlucci**. I agree with you, sir, nothing is more important to effective procurement than the quality of the two people.

There is often a tendency to want to look at boxes and move boxes around and change the organizational structure. People are far more important than the organization. Good people can even make a bad organization work. A good organization will not work with poor people.

We are trying to implement a modern technology procurement program with a 19th century civil service system. We have demonstrated through the China Lake experiment that changes in the system can improve the quality, and your legislation goes a long way toward broadening that experiment.

I would be prepared on the basis of that experiment to move into an operational system, but I guess that is not feasible. So we welcome the 100,000 person experiment, the ten experiments.

Senator **Bingaman**. On another issue, one of the frustrations that Mr. Godwin had when he was in the job of Under Secretary for Acquisition, as I understood it, was the problem of his authority or interaction with the Service Acquisition Executives in each of the various services. Particularly, I think that was a serious problem with regard to the Navy.

My understanding of the Packard Commission recommendation was that the Under Secretary for the Department of Defense should approve the appointment of the Service Acquisition Executives.

Mr. Godwin testified to us in this committee that that was never done in his case. He was essentially informed as to who those folks were. I also understand the Secretary of the Navy appointed himself as the Service Acquisition Executive, as a fairly obvious way to undermine that new structure.

I would be interested in knowing if you have in place today procedures or regulations or some means to assure that those Service Acquisition Executives are in fact appointed with the approval of the Under Secretary for Acquisition and that we do not have the possibility of a service Secretary in the future appointing himself to that job?

Secretary CARLUCCI. Well, there is no service Secretary in the job. Perhaps the best way I can answer that question is to ask the Under Secretary himself to answer it.

Senator BINGAMAN. OK.

Dr. COSTELLO. In each of the cases where there has been a new appointment since I have been in the job, the service Secretary has come to me and we have discussed the candidates, and I said I concurred, basically, with their choice.

I might go further than that. The Service Acquisition Executives and I have weekly meetings. We talk about policy, we talk about strategy, we talk about implementation, where they are.

So we talk about the critical issues that are important to us to get the reforms identified by the Packard Commission, as well as the reforms that both the Secretary and I have been strongly supporting.

Senator BINGAMAN. Mr. Secretary, one of the things that Mr. Bowsher said yesterday that was of particular concern to me, and I am sure it will be to you, is—just a couple of sentences. Let me quote them to you. He says:

> In addition to these scandals, I think the other shoe will probably fall soon, namely many big-cost overruns. I suspect the Stealth airplane program, the Navy shipbuilding program, and other programs which have to be stretched because of budget constraints will all result in very large cost increases that the Congress and taxpayers will have to finance.

I asked him about that and he said that that was a result of the fact that good information was not on a regular basis flowing back to the Secretary. And he cited the case of Secretary Laird when he took the job becoming aware of the cost overruns on the C-5 and demanding that any other serious cost overruns that existed be brought to his attention at that time.

He said that his view was the only way the Congress could be made aware of that information is if you would make that same kind of demand, that any cost overrun situations that are there waiting to be announced are brought to light, so that we have that information before we start the next budget cycle.

Secretary CARLUCCI. Well, there is of course, Senator Bingaman, a whole procedure under the SAR procedure which your chairman played a very important role in initiating, where we report cost growth in our major weapons systems to the Congress, and we are obliged to send special reports where cost escalation exceeds certain parameters.

Senator BINGAMAN. Let me interrupt to say, I aked him about that. He indicated that in his view the SAR has ceased to be a useful tool in reporting these kinds of cost overruns.

Secretary CARLUCCI. Well, I do not fully share that view, and I think we have tended to put too many programs on the SAR and then tended to put a lot of constraints on it. But nonetheless, I think it is a useful tool.

Mr. Bowsher is speculating on the future. If you take a SAR report in 1981, the cost escalation was about 14 percent. The last two SAR reports have been below zero. So there is virtually no—there are costs underruns.

Now, that being said, the way we got the 14 percent down was through such devices as baselining, multi-year procurement, procuring in economical quantities. The last is particularly important.

In a period of descending budgets, I and my successor have a great deal of difficulty in maintaining economical quantities. We managed to do that pretty well in the 1989 budget. In the 1990 budget, my own sense is that that is going to be more difficult to maintain.

You have only got a couple of fundamental choices. You can terminate major weapons systems. In many cases that does not save you money, particularly if they are in production. You have termination costs, and you sacrifice the system as well.

Or you go into personnel, readiness, and sustainability in a period of decreasing budgets. You cannot take down that much force structure. So I think I am concerned about that possibility in the future.

But certainly, in the present there are no grounds to argue that there are endemic cost overruns. Indeed, there are grounds to argue that we have made cost underruns.

Senator BINGAMAN. My time is up. Thank you, Mr. Chairman.

Chairman NUNN. Thank you, Senator Bingaman.

Senator Quayle.

Senator QUAYLE. Thank you, Mr. Chairman.

Mr. Chairman, I would ask unanimous consent that an opening statement of mine be inserted in the record at the appropriate place.

Chairman NUNN. Without objection.

[The prepared statement of Senator Dan Quayle follows:]

PREPARED STATEMENT BY SENATOR DAN QUAYLE

I congratulate the chairman for calling these hearings on the acquisition process. It is a vital subject and it is essential that the committee exercise its oversight responsibility in light of the grave charges concerning that process which are the subject of the current investigation.

We need to look carefully at the appropriate response to what has been happening. Published reports suggests that we have old-fashioned bribery and corruption against which we have had laws since the establishment of the Republic. The best response to such crimes is to prosecute them to the hilt. Criminal penalties are enacted both to punish the guilty and to deter future offenders. We must not underestimate that deterrent effect.

However, we must also be vigilant to see whether the evidence (which is not in yet) shows weaknesses in the acquisitions system beyond the fact that men succumb to temptation.

Since long before the current investigation was made public, I have believed that we need to make substantial reforms in the Defense Department procurement process. As chairman of the Defense Acquisition Subcommittee, I shepherded major changes in the acquisitions system into law. These changes were bipartisan and were founded on the recommendations of the Packard Commission.

However, many of these changes did not go far enough and some were not enacted at all. Probably the greatest gap between the proposals I made and what became law was the failure to establish a defense acquisition service—a cadre of highly trained, highly motivated, and well compensated procurement experts who would be rewarded for excellence. Effective management of the procurement process will not prevent bribery and corruption—but it will deter it and expose it before too much harm is done.

The record may show that other procurement reforms are necessary—but let us not enact laws just for the sake of it or pretend that a new criminal penalty will ensure that the 10 commandments will no longer be broken.

What is it that we need to know before we try to enact legislation? First, we need to analyze whether the crimes that are alleged could have been prevented. Are they due only to avarice or does the system give the avaricious a special opportunity? Only if we find that the latter is true should we legislate.

The focus of the investigations seems to be on the role of consultants. Does our legal framework governing the procurement process deal adequately with the appropriate role for consultants? Would a restriction of their role benefit the public interest? Is greater information needed on their activities?

We also need to put this investigation into perspective. How does the extent of the illegal activities alleged compare to the record of the past few years? in the number of persons investigated? indicated? convicted? the dollar amounts involved?

So far we have none of that information and we should not assume there is massive wrongdoing before the investigation is concluded or indictments or convictions obtained.

It is not easy to say "slow down" when it is proposed to punish bribery and corruption. It may be good politics to say "throw the rascals into jail" even when we have not yet identified any rascals and when a jail term already awaits them. But even if it is not good politics, I suggest it is good public policy to analyze the facts and the issues before we jump to conclusions and enact new legislation.

Senator **Quayle**. Mr. Chairman, first I want to commend you for the tone I detect and interpret in your remarks establishing for this committee—the tone that I detect from you and also the ranking member is that we are going to examine this, we are going to get all the facts in, we are not going to be rushed to judgment.

We had Mr. Bowsher yesterday, the Secretary today, and we will see what in fact we have before us. If in fact the facts bear out that this is corruption and bribery, it is as old as the Republic. It is nothing new, unfortunately. It does not mean that we should not prosecute fully to serve as a deterrent in the future, and that is I am certain what will happen.

But I do want to congratulate you for at least the way I interpret the way that we are going to proceed.

I would like to remind my colleagues a bit about the former Under Secretary for Acquisition, on how frustrated he was in this deputy position. I remember in the testimony of Mr. Godwin I asked him point blank, was there any time that he took a request to Secretary of Defense Cap Weinberger that was rejected.

The answer came back, no, that every time that he took a problem to the Secretary, the Secretary supported him. Now, there may have been frustrations elsewhere in the system. But as far as having authority and getting authority, certainly the record will bear out that he had that authority from the former Secretary of Defense.

This concern about the deputy, this was not a recommendation of the Packard Commission. This first came up, as a matter of fact, in the subcommittee I chaired. Initially I was somewhat relucant to put it in the legislation.

It was only after the personnel was identified who was going to take this position and truly in fact thought that he might need a deputy, and under those circumstances, if you want a deputy, I think it certainly goes to the individual. It is certainly a choice to make.

But this was a congressional initiative. This was not a Packard Commission recommendation, which we hail as something that is very important.

Mr. Secretary, my first question is, as you look at this and you step back, it appears from the allegations that most of the problem is in the Navy. There are others, but the majority of the problem appears to be there.

Is there something unique about the procurement system in the Navy that would create a climate for these allegations that have been made? I am just trying to, from the viewpoint right now, is there something unique about the Department of the Navy that would tend to be different, that might be vulnerable to these types of allegations?

Secretary CARLUCCI. That is a very hard question to answer, Senator Quayle. The procurement systems are somewhat different due to the different nature of the weapons they acquire. Acquiring ships is very different than acquiring airplanes or missiles or even tanks.

The Navy system I think at the same time is a much more centralized system, where they tended to place more emphasis on competition. Whether that had a bearing on what happened is too early to tell until all the evidence is in.

The Navy also tends to make more extensive use of consultants. But here again, all the consultants that seem to be implicated in this investigation are consultants to defense contractors and not to DOD itself.

So I am really hesitant to give you even an off the cuff answer to this, to your question until more of the evidence is in. I do not know if my colleagues would like to respond.

Senator QUAYLE. Is there anything, Mr. Costello, that is unique about the Navy, the current system, that would create a different type of environment, that these allegations made would seem to be more oriented to there than elsewhere?

Dr. COSTELLO. There is no obvious point of departure from the Navy system. They follow the same regulations. They work through the same defense regulations that we do. They do refine them for the Navy, but their overall structure is controlled and monitored by the same group of people that do the activities for the Air Force and the Army.

There is no obvious problem except that perhaps there is a group of contracts in the electronics industry, say relatively small, maybe in the tens of millions of dollars range, rather than the major contracts in the billions of dollars range, upon which people first focused. That may be more of an industry thing than it is a service situation.

Secretary CARLUCCI. The Navy tended to do something with which I disagree. This was during the period I was not in the Pentagon. They tended to use fixed-price contracts for R&D, and that has now been changed.

Now, whether that has contributed to this or not I don't know.

Senator QUAYLE. I would be interested in that question, because there seems to be more there than elsewhere. Now, I suppose some conclusion that at least I could make is maybe it is individuals more than the system. If in fact that is the case, then that is something that we ought to know.

If there is not a discernible difference in the procurement process between the three services, then I think we have to jump to that type of a situation.

Secretary CARLUCCI. From what we have been able to learn from the prosecutors, it was individuals, or at least that is what the Justice Department is telling us.

Senator QUAYLE. Let me just say that I have listened to Mr. Bowsher, I have listened to you, and I have about four areas where I think that there is legitimate concern and interest. Three out of the four is something I think that perhaps you could do internally as you look at this.

The one that you can't is the one that Senator Bingaman talked about, and that is the acquisition corps. If you recall, I know that Senator Bingaman as a matter of fact was very instrumental in the 1986—we had this in the defense authorization bill to increase that.

As a matter of fact, it was very similar to the legislation. And it was defeated on the floor. There was an amendment to strike that on the floor. It was a very close vote.

You are going to need—you need some help from the Congress, and I certainly agree with your point as far as the restriction on the personnel system. There is a huge restriction. You do need our help.

That is the number one area of concern that I continue to have. I had that back when I chaired the Acquisition Subcommittee.

The other three seem to me that you might be able to do something. I just mentioned them for your interest.

First, perhaps some more disclosure from consultants on who these consultants really work for, both ways. I think that there are probably some things that could be done.

Second, the way we go about this best and final offer, this negotiated settlement, because that is where the inside information seems to be of very paramount importance. If they can get that inside information, however they get it, they can go out and trade it off and make lots of money and things of that sort.

But I think that is a concern of mine.

And finally, how can you go about instituting a voluntary code of ethics with business. You have only, I think, 46, who have signed up to this code as you mentioned. But there is absolutely no incentive for any defense contractor, for their own self-protection in the political environment that they find themselves in, to have an established code of ethics that they implement and enforce.

I am with you. I do not want to draw this thing up and have the Government go in there and check every *t*, whether it has been crossed. But I do think that this is something we could pursue.

So three out of the four areas that I identified I think can be done somewhat internally. We can hopefully give some help on this acquisition. But I hope that the spirit of our review is like what the Packard Commission really concluded when we looked at this the other time, and that is, you know, legislation can work both ways.

If you recall, and you were on that committee, one of the strongest requirements or recommendations of that Packard Commission was that there was not a need for a lot of legislation, that there were some things that could be done internally.

Secretary **Carlucci**. I agree with that and I think your points are well taken. And they are points that our task force has under review.

We have no real controls over contractor consultants, the contractor's use of consultants, although they are reimburseable costs. So we may be able to exercise some influence in some way there, and that is one of the things that the task force is looking at.

As I indicated in response to Senator Cohen's question, I myself have some questions on best and final offer, and we're examining that, and voluntary code of ethics. I plan to send a letter to contractors shortly, and I think that is one of the things that we could include in the letter, urging them to adopt such a code.

I must say David Packard has been very helpful on this. He personally has approached most of the major contractors and urged them to sign up. And I am working closely with David.

Senator **Quayle**. Thank you, Mr. Chairman.

Chairman **Nunn**. Thank you, Senator Quayle.

I believe Senator Shelby is next.

Senator **Shelby**. Thank you, Mr. Chairman.

I have an opening statement and I ask unanimous consent that it be made part of the record.

Chairman **Nunn**. Without objection, it will be made part of the record.

[The prepared statement of Senator Richard Shelby follows:]

Prepared Statement by Senator Richard Shelby

I would like to thank the distinguished chairman for scheduling this set of hearings. I believe that all members of the committee realize the significance and importance of the Pentagon procurement scandal. However, most of the evidence remains under seal in Federal Courthouses. With this in mind, we need to proceed cautiously. We do not need to conduct our own investigation at the expense of current inquiry.

What we can do is look at the system. If it needs to be fixed, then how do we fix it? Do we need more regulations, or less regulations? Have we made the system so complex, that contractors must seek outside consultants, who have the expertise and contacts within the Pentagon? Should we give our senior executive services personnel more incentives to stay within the system or is the promise of riches or huge expense accounts just too inviting?

Mr. Chairman, America has been hit with so many scandals, the people of this country are beginning to find them commonplace. The Members of Congress, as well as all the men and women of the business world, are not surprised when they hear of an illegal sale of a product or an illegal transfer of funds.

Only a few years ago, the act of cheating on one's taxes seemed to be a major offense. But during the 1980's, we have been confronted with the dealings of Ivan Boesky and Robert Levine. Only 1 year ago, members of a select Senate committee were discussing the details of Irangate, an investigation of monumental proportions which centered on the alleged illegality of arm shipments from the United States to its worst enemy, Iran.

My friends, these scandals would probably be humorous if they were not so tragic. Many of you in this room have fought in battle for America in order to uphold the freedoms that you so dearly possess under the Constitution. We are the longest living democracy in the world, yet there are some people involved in government who are, either knowingly or unknowingly, undermining everything these veterans have fought for.

No matter if you are a drought-stricken farmer, a high-rolling securities trader on the New York Stock Exchange, or even an exhausted civil servant working in the District of Columbia, *you must learn how to play by the rules.* You might not like the way the rules look on paper, but you cannot and should not break a law and then claim that you are doing what is best for the American people. The United States is not a perfect place, but it remains the shining democracy on the planet

Earth because of the laws that 99.99 per cent of America's men and women struggle to uphold. Yet, when you turn on the evening news, the only celebrated members of our society is that .01 per cent which is doing damage to American ideals and values.

In closing, let me say that I have a variety of emotions regarding this affair. Most of all, I am ashamed, dejected, and most of all, angry. Every day, it seems, the American people discover another reason to distrust the government. I am hopeful that we will learn from our mistakes.

Thank you, Mr. Chairman.

Senator SHELBY. Mr. Carlucci, it seems to me from observing and being briefed on what has gone on in the acquisition process that the restoration of public confidence in the defense acquisition process should be the central problem that you try to attack. I believe that you are doing this.

Something that bothers me a little bit and maybe more than a little bit was a statement earlier, I believe by Mrs. Buck. I wanted to correct this if I misheard her. She mentioned the level of taint regarding these contracts.

I would like to know, Mr. Secretary, first, and with your counsel here, what you mean by the level of taint, assuming fraud is taint? It is interchangeable to some extent here. It reminds me of someone being a little bit pregnant, that if there is fraud here there is fraud here.

I believe to restore public confidence in the system you are going to have to purge this. I would like to hear your comments. First your counsel, I suppose.

Did I hear you wrong on that, to begin with?

Ms. BUCK. What I was talking about is, as we go through this process and the facts of the investigation unfold, we will do a contract by contract review to determine what facts we have that might impact on a particular contract. And until you get the evidence, the actual evidence, which we are now starting to receive as the affidavits are unsealed, it is very difficult to prejudge exactly whether we have a problem under the terms of the contract.

That is what I was focusing on—until we see those facts we will not know how serious the problem is.

Senator SHELBY. I agree with you on your analysis, and the probe is under way and it is not complete and will not be complete, and I understand that. But if you get into fraud and if you find fraud, I say to you you cannot reward fraudulent conduct.

You cannot reward anybody with it, because you undermine the whole public process and public confidence. That is the point I was trying to make.

Do you agree with that?

Ms. BUCK. Well, I think in principle we certainly do not want to reward fraudulent activities.

Senator SHELBY. You do not want to, but will you?

Ms. BUCK. I think that that is the purpose of our process, to see that we do not. And you are talking about various things here, one of which is of course the Justice Department's ongoing investigation. We are doing everything we can to support the Justice Department in that fraud investigation, to see that fraudulent activity is not rewarded, and that in fact the people who have engaged in wrongdoing are punished appropriately for that wrongdoing.

Senator SHELBY. Mr. Secretary, do you want to comment on that?

Secretary **Carlucci**. Well, just to say that while fraud obviously is an absolute term, you have to look at the degree of involvement and knowledge of the senior officials of the firm as well. It may be that some information illicitly gained was passed in a legitimate way.

Senator **Shelby**. Did they profit from fraud?

Secretary **Carlucci**. And did they profit from it. I think that is what we have to look at.

Senator **Shelby**. Mr. Secretary, one other question while I have a little time, regarding the Navy and the Air Force, which seems to be the focus of this early probe, as opposed to say the Army.

You did mention—I believe you are totally right on this—that what they are buying is different, Navy, Air Force, Army, and so forth. But the people are the ones that commit fraud in a system. I believe you mentioned this.

You can have the best system in the world. Was the Navy lax or seemingly so in the selection of the personnel that were going through the acquisition process? Is the real problem one of people?

Secretary **Carlucci**. There is certainly the possibility of that, Senator Shelby. I think it is too early in the investigation to make those judgments. I have taken certain actions with respect to individuals, three consultants and one individual in the Department of the Navy. But I certainly do not want to imply guilt before any evidence is in.

Furthermore, it is not my job to determine guilt.

Senator **Shelby**. You are not the Justice Department.

Secretary **Carlucci**. That is the Justice Department's job. One of the things that we ought to do if this indeed does turn out to be a people problem is to review, to make certain that there is adequate scrutiny.

Now, Presidential appointees go through the FBI check and fairly rigorous scrutiny, conflict of interest forms and all of that. At the civil service level, we do not have the same kind of scrutiny, and maybe when we come to the case of contracting people we ought to have more in-depth procedures.

That is one of the things we will have to look at.

Senator **Shelby**. Well, if the word went out that there was fraud by *x* company, and it did not matter how large they were, why not suspend them, period, from doing business with the Government? Make an example out of them.

Secretary **Carlucci**. I am perfectly willing to make examples.

Senator **Shelby**. If it were justified.

Secretary **Carlucci**. What I have to weigh, coming back to the point both you and I made earlier, I am not the Department of Justice. My job is not to punish companies. My job is to protect the national security interest and to look at the system and see how I can best protect the system, how I can best equip my troops.

Senator **Shelby**. Including the integrity of the system.

Secretary **Carlucci**. You are quit right, including the integrity of the system. I also have to weigh these other factors, and that is what we will do as we go through this process.

Senator **Shelby**. My time has expired. Thank you, Mr. Chairman.

Chairman **Nunn**. Thank you, Senator Shelby.

Senator Dixon.

Senator DIXON. Mr. Secretary, the Packard Commission report in 1986, which you signed, stated:

> There are certain common characteristics of successful commercial non-governmental policies and projects: sharp, unambiguous lines of communication among levels of management. Responsibility for acquisition policy has become fragmented. There is today no single senior official in the Office of the Secretary of Defense working full time to provide overall supervision of the acquisition system.

The report then recommended the creation of an Under Secretary with powers to "supervise the performance of the entire acquisition system." And as you know, I was the principal sponsor of legislation that created the Under Secretary of Defense for Acquisition.

Now, Webster's Third New International Dictionary treats the word "supervise" as follows:

> To coordinate, direct, and inspect continuously and at firsthand the accomplishment of; to oversee with the powers of direction, decision, implementation of, another's intentions.

I ask you if all of that is not something at least at odds with your statement on page 8 today where you say it means being suspicious of proposals that would further separate acquisition responsibilities from the military users by taking away major functions currently under the services and centralizing them under our Under Secretary of Defense for Acquisition.

Is it not a fact that what you recommended in the Packard Commission and what our legislation attempted to undertake was absolute supervision, direct line authority by the Under Secretary of Defense for Acquisition over the service acquisition chiefs and people underneath them?

Secretary CARLUCCI. I think the Packard Commission's recommendations—and as you point out, I participated in the deliberations—has been met by the current structure. I think the Under Secretary for Acquisition does have the authority to supervise.

I think it would be a mistake to simply cut the service Secretaries or the uniformed services out of the process.

Senator DIXON. Would you agree that there has been an attempt on many occasions by them to deter the intentions of the Under Secretary of Defense for Acquisition? For instance, I remember when John Lehman was Secretary of the Navy he made himself acquisition chief for the Navy.

Secretary CARLUCCI. Senator, I will go one step further and I will say that there are attempts on the part of the services to deter the intentions of the Secretary of Defense.

Senator DIXON. I am shocked to hear that, Mr. Secretary. But I always suspected as much.

But the point is here that, you know, there are some of us who you might think are antagonists now that have considerable confidence in you, Mr. Secretary, and both of the people with you here. I think the Under Secretary of Defense for Acquisition is trying to do a formidable job.

I would suggest he cannot stop a major weapons system or make particular changes if there is a lot of opposition inside one of the branches of the service.

Secretary CARLUCCI. Oh, I can assure you he can.

Senator DIXON. You would make that statement to me, sir?

Secretary CARLUCCI. Absolutely, and I think he will back me up.

Senator DIXON. Would you, Dr. Costello?

Dr. COSTELLO. I think even our directive says that I have direct authority over the service Secretaries in acquisition matters.

Secretary CARLUCCI. That is clear, and the Packard Commission recommended that. We had quite a debate over this, and we said in protocol order he would rank below the service Secretaries, but in terms of acquisition, the acquisition process, he would rank with services Secretaries, quite explicit. I am not sure of the exact language.

Dr. COSTELLO. I think the real key is that the Secretary has to have an organization that can come to him with the appropriate balance between operations, economics, the physical structure, and the acquisition. That is the technology, the procurement, the ways we do things.

And even on the boards that are set up, even on the defense resources board, we have four members that are from acquisition on that board. We have a very strong influence on all the decisionmaking.

We cannot superimpose our perspective over an operational need that may be in the Secretary's mind and judgment more important. And that is a case that we bring to the Secretary's——

Senator DIXON. Is your interpretation, Dr. Costello, and more importantly, with no reflection on you, is it the interpretation of the Secretary himself, that the service acquisition chiefs in the separate branches of the service are subject to your supervision, authority, and control and direct line authority under existing law?

Secretary CARLUCCI: Let me comment on that. When you say direct line authority, that has certain implications.

Senator DIXON. Of course it does. That is why I say it that way.

Secretary CARLUCCI. The implication is that you are moving them out from under the service Secretaries. What he has is total authority over policy, over the process, and total access to the implementation of the system. He sits on the defense acquisition board where the systems are reviewed, or he cochairs it.

So he has the authority to move in and stop a system. Now, the service Secretary has to continue to play a role. So in a sense, he has some authority over his people as well. So you have got a forum of collegial management here.

But I think the lines of authority for the Under Secretary for Acquisition are very clear. I should also make it clear in the final analysis that if there is a dispute over weapons system *X* and the Under Secretary for Acquisition says, no, this system should not go forward, the service Secretary obviously has a right of appeal to me.

That has not happened. But I can assure you I would give great weight to the views of the Under Secretary for Acquisition.

But fundamentally, the Secretary of Defense has to be responsible for the system.

Senator DIXON. Thank you.

Mr. Chairman, may I ask one more question? My time has expired, but I cannot come back for another round.

Mr. Secretary, as you know, my bill is in two parts. One is the centralized authority of the Under Secretary of Defense for Acquisition. We can continue to pursue that at a later date.

The other, as you know, is setting up a codified standard of conduct for people inside the Department of Defense and those in Industry with respect to these many involved defense contracts that take place, and then suggesting that at the end of the contract there is a certification on both sides that this standard of conduct has been adhered to by participants on both sides, with of course a violation of a criminal statute if you violate your oath in respect to certifying this.

It would give a lot of administrative authority to the Secretary of Defense to act both against people in his own Department and against people in the industry, to set aside contracts and otherwise take steps that would protect the interests of Government and the taxpayers.

And there has been some talk. I have heard a lot of talk about voluntary standards of conduct, for instance, in the industry. My thought about that is, going all the way back to the Ten Commandments, we have found that voluntary standards do not matter much for people who do care.

I was just wondering what your response is to at least the concept, not the specificity of the second part of my legislation, but the concept of some kinds of standards of conduct that are involved in the contractual negotiation process that have to be adhered to to continue the viability of the contract upon some violation being later found.

Secretary CARLUCCI. We would be delighted to work with you on that, Senator Dixon, as well as on the authority of the Under Secretary for Acquisition. We are not locked into concrete on either of them.

You made the comment that standards do not matter for people who do not care. I would raise the same question. For people who are going to violate the law in any event, would signing a document make any difference?

Senator DIXON. Except that you could take legal action there specified in the bill and negate the contract and punish the people. In my bill, you would put the person out of business working as a Federal employee. You could do away with the right of the company to do business with the Government in the future.

Secretary CARLUCCI. There may be ways where we would want to strengthen the authority of the Secretary of Defense to deal in this area. I would not like to make him a law enforcement official, though. We have to bear in mind that the job of the Secretary is to protect the system and field the weapons, and not to punish criminals.

But there may be ways that we can do this more effectively. I am a little gun-shy of the amount of paperwork this would create, but we would like to work with you on it.

Senator DIXON. Thank you.

I would like to put my statement in the record, Mr. Chairman.

Chairman NUNN. Without objection.

[The prepared statement of Senator Alan Dixon follows:]

PREPARED STATEMENT BY SENATOR ALAN J. DIXON

Mr. Chairman, we are pleased to have Secretary of Defense Frank C. Carlucci with us today as we begin our review of the defense acquisition process.

Just last Friday I introduced Senate bill S. 2621, the Department of Defense Procurement Improvements Act of 1988. This legislation establishes the Under Secretary of Defense for Acquisition as a true acquisition and procurement czar within the Department of Defense. The legislation centralizes authority and responsibility for acquisition policy in a single office. It also establishes parameters for contractors, consultants, and government officials involved in government contracting.

I read with interest an article by John Cushman, Jr. in the Sunday, July 10, 1988 edition of the New York Times that "Defense Secretary Frank C. Carlucci and his Under Secretary Robert B. Costello are opposed to Mr. Dixon's legislation." Mr. Cushman states that Mr. Carlucci and Dr. Costello feel that my bill "goes too far" and that procurement problems can only be addressed through new regulations that the Pentagon plans to implement. I have heard that before!

As the chairman knows, I introduced the legislation that initially created the office of the Under Secretary of Defense for Acquisition. At that time I had to engage in battles with the Secretary of Defense and the service Secretaries. The original bill gave the Under Secretary complete responsibility for supervising the entire defense acquisition system but the Pentagon resisted this essential reform and a weaker version of my legislation became law.

Now Secretary Carlucci, in a Sunday July 10 Washington Post story, was quoted as saying that "the procurement process has become exceedingly cumbersome and complex—characterized by multiple decision points, each of which provides opportunities for congressional micromanagement and influence by special advocates." Yet just a few weeks ago his own spokesman, Dan Howard, was quoted as saying "the Secretary is confident that we have a very solid, adequate acquisitions process. . . . We feel the overall mechanism is sound." I hope the Secretary will explain this contradiction today because he is beginning to sound like his predecessor. When Secretary Weinberger found things going wrong in the Department of Defense, he blamed Congress.

I would like to remind the Secretary that, as a member of the President's Blue Ribbon Commission on Defense Management, he signed the final report submitted to the President on June 30, 1986 which stated: ". . . there are certain common characteristics of successful commercial and governmental projects—short, unambiguous lines of communication among levels of management . . . responsibility for acquisition policy has become fragmented. There is today no single senior official in the Office of the Secretary of Defense (OSD) working full-time to provide overall supervision of the acquisition system . . ."

The report then recommends the creation of an Under Secretary with powers to ". . . supervise the performance of the entire acquisition system . . ."

Mr. Chairman, we cannot totally legislate away greed and corruption. But we must do everything possible to correct the inherent inefficiencies of the current system and reduce the potential for abuse. The cause of national security should not be a shield for incompetence, mismanagement, corruption, and cronyism.

I look forward to hearing Secretary Carlucci's views on the defense acquisition system.

Chairman NUNN. Senator Levin.

Senator LEVIN. Thank you, Mr. Chairman.

Mr. Secretary, welcome, and to everyone else.

In looking for the causes of the current problems that we have, I would look at four possibilities:

One would be, obviously, flat-out crimes. That is hopefully going to be taken care of by the Justice Department. We will put that aside.

Second, the question of whether our laws and regulations are strong enough or whether or not they have got loopholes. There I want to focus for a few minutes on that particular piece of our problem.

Third is whether or not we have adequate enforcement of existing laws and regulations, and I want to spend a few moments on that.

And the fourth would be the structure of our procurement system, and I want to spend a minute or two on that.

But other than the overall question of personnel in the system, which is obviously important, it seems to me those are the four things we ought to be looking at. One is the Justice Department looking at crimes, and the other three are things that hopefully you are going to be looking at: loopholes, weaknesses in the laws and regulations, inadequate enforcement of existing laws and regulations, and the structure that we have.

Secretary CARLUCCI. I agree with all those.

Senator LEVIN. The loopholes, let me give you an example of a problem that seems to me is a real one and that we talked yesterday with the GAO about, and we have indeed talked to Mr. Vander Schaaf (the Deputy Inspector General in the Defense Department).

And that is the question of consultants who are under contract with the Defense Department to give us advice, and our failure to require them as a routine matter to disclose who their other clients are, so that we can judge whether or not there is either the appearance of a conflict or a conflict of interest between the advice that they are giving us and advice that they give to their other clients.

What the media has focused on, and rightfully so, so far is the problem of consultants to private companies who obtain information improperly from us, through bribes or otherwise, and then give that information for a price to their clients.

Secretary CARLUCCI. Right.

Senator LEVIN. What I am asking about is exactly the reverse, where we hire a consultant, we indeed pay a consultant to give us advice, the consultant has access to that advice and other inside information, but that consultant also has other clients and we do not know as a routine matter who those clients are.

Now, there are some specific circumstances where we might—he might be required to disclose to us, for instance if in the opinion of the consultant there is a conflict of interest. Then that consultant would be required to disclose to us.

Secretary CARLUCCI. I am informed by my general counsel that consultants are required on form 1555 to disclose their other clients.

Senator LEVIN. In other words, what you are saying is that every consultant that signs a contract with us is required to disclose who the other clients of the consultant are?

Ms. BUCK. You are talking about consultants who work directly for the Defense Department?

Senator LEVIN. That is right. I am not talking about people in advisory boards.

Ms. BUCK. In fact, I doubled checked on that question myself this morning. I wanted specifically to know not only did they disclose the firm that they worked for, but were they disclosing their clients.

I was advised that specifically they do disclose their own clients, as well as the firm that they are working for. So if they work for XYZ Corporation plus they are specifically advising certain companies, they disclose that on form 1555.

Senator LEVIN. Now, I am advised that is only if they believe that they have a conflict of interests.

Ms. Buck. No, that is not how it was described to me.

Senator Levin. All right. I think there is a difference on that. It is a very critical difference. We have checked it out.

Ms. Buck. No, I think that is a very good question, and so that is why I decided I would ask it myself, to double check on that.

Senator Levin. All right. We have done some checking on it. We believe it is only where the consultant believes there is a conflict of interest, that then there is a requirement of disclosure. There is not automatic requirement of disclosure for all consultants.

But in any event, we can check that out. If there is not such a requirement, then you would then go along with a proposal which we are drafting to require such a disclosure, is that fair enough, at least tentatively?

Ms. Buck. Certainly.

Secretary Carlucci. I do not have any problem with that.

Senator Levin. That may or may not be a kind of a loophole.

Let us go to the next one, and that is the question of enforcement of existing laws. We have recently completed a report which shows that 98 percent of conflict of interest cases referred to by the inspector general in 10 different agencies, not just DOD, from 10 different agencies, that go to the Justice Department for criminal prosecution were not prosecuted.

Ninety-eight percent of conflict cases referred to the Justice Department as having adequate basis for prosecution are not prosecuted.

Another problem. The defense procurement fraud unit set up by the Justice Department does not even keep track of its cases. We cannot tell how many cases are referred to the defense procurement fraud unit in the Justice Department and what the disposition of those cases were.

Another example. The Office of Government Ethics issued a rather scathing analysis 2 years ago of the Navy ethics enforcement program. That was under existing law. I do not know if you are familar with that OGE report or not. You should—if you take a look at it, it is a scathing indictment, a 1986 report, June 9, 1986.

And you should give us a response to that for the record.

The Governmental Affairs Committee looked at the enforcement of the conflict of interest provision for the DOD advisory committees, particularly inside the SDI office. And frankly, we found a defiance of the requirements of the Federal Advisory Committee Act over and over and over again.

The SDI in setting up advisory committees, which then put people under conflict sanctions and bonuses—it was ignored by the SDI office. And that was extremely disturbing in Governmental Affairs, to us.

The bottom line here is that it seems to me that at least in general, we have not adequately enforced existing laws and regulations. There are exceptions. We have on some places adequately enforced them. But too many times, we have the regulations on the books.

I just pick out FACA, one example, Advisory Committee Act laws, which has been absolutely fundamentally ignored. And then when it is pointed out, that advisory committee will be terminated and then another advisory committee set up.

That is something which disturbs me and I know would disturb you. If you were satisfied that that conclusion were true, you would be equally disturbed as I am.

But I think we ought to look at that as well, so that we not only look at structure. And Senator Dixon and others have pointed out the question on the Under Secretary. By the way, I am convinced—we have reviewed the history of the Under Secretary again. We shed blood over the creation of that office.

You, Dr. Costello, have all the authority you need to act on specific contract matters if you want to exercise it. You can use your consensus approach all you want and it is fine when it works. But one of the reasons it will work is that you have the authority to enforce your decisions.

I am out of time, but let me just tell you that, if there is any doubt in anyone's mind that you can direct specific contract actions if you so decide, we will give you that background material again.

The bottom line, I think we have work to do in all of those areas: the enforcement of existing regulations, plugging up loopholes where they exist—we may or may not be right on this one; we think we are on some other ones—and on the structure.

Secretary CARLUCCI. I would agree with that.

Senator LEVIN. My time is up, Mr. Chairman.

Chairman NUNN. Let me ask a couple of questions as we begin the second round.

We have implemented a new procedure in the last couple of years, that you are very much a part of, where we have you look over the financial records of a potential nominee or a proposed nominee by the President for a top DOD position. And you certify now, to us, that you have examined those records and you see no conflict of interest, or you perhaps see a conflict, depending on the case. Is that right?

Ms. BUCK. Yes, sir; that is correct.

Chairman NUNN. Does that impose any undue burden on you?

Ms. BUCK. No, sir. I am happy to do it.

Chairman NUNN. Does it get you more involved in a detailed examination of potential conflicts than would otherwise be the case, or are you doing that anyway?

Ms. BUCK. I think we have always done a pretty detailed review in terms of the financial disclosure forms, working with the Office of Government Ethics and the White House. But to the extent that it is helpful to you in your overall nomination process, I think we are happy to do that.

Chairman NUNN. What about FBI reports? Do you see FBI reports on top Department of Defense nominees?

Ms. BUCK. No, sir, I do not.

Chairman NUNN. Would it be helpful for you to see those reports on behalf of the Secretary? In other words, you are looking at financial information in conflict of interest that could be there, but you do not get to look at an FBI report to determine if the individual involved may, in fact, be someone suspected of fabrication, lying, distortion, and so forth. What would that information do for you in your job?

Ms. BUCK. It is currently reviewed, of course, by the FBI and by White House counsel, and so my review would be an additional review. Personally, I have always felt very comfortable with the process of White House counsel——

Chairman NUNN. But the White House counsel does not review the financial information?

Ms. BUCK. No, sir; that is not correct. The White House counsel's office does do that, in addition to my review.

Chairman NUNN. Are they supposed to look at conflict of interest and financial information?

Ms. BUCK. Yes, they do. Actually, there ends up being three entities within the Government looking at that. You have the White House counsel review, you have Office of Government Ethics review and then you have a review by my office as well.

Chairman NUNN. What would be wrong with having you also review the FBI report, since the individual is going to be working for the Secretary of Defense, and certainly some information that might be relevant to the individual's integrity could potentially be in that report?

Ms. BUCK. As I said, there would not be anything wrong with that, I have just always felt comfortable with the process of relying on the FBI, which, based on my experience in working with them over the years, has been an exceptionally good one, and White House counsel.

Chairman NUNN. When you get a new administration in office, whether it is a Democratic administration or Republican, the administration will have to deal with all these nominees for all these departments all over town, not just defense. You have a small White House counsel's group down there, they are supposed to be familiar with committee procedures which vary all over the lot in terms of whether we get the FBI reports.

We hope we now have a system in effect, but it varies. You have people who are doing the detailed scrutiny on financial information in the Department of Defense and potential conflict of an employee never seeing an FBI report.

You have, in several cases, not just recent cases that have come to my attention, of the White House counsel's office not going into information that may very well be in an FBI report that has allegations that are never checked out.

The whole system does not seem to work very smoothly. I have had the FBI come up to me right after we confirmed a top nominee—this happened to be a Democratic administration—and ask me what I thought of the individual. They were just starting their report, after the Senate got through confirming.

The process has got to be readdressed. It simply does not appear to be working. And I include ourselves in that.

Ms. BUCK. Well, in my opinion, what I think is important is a good FBI check in every situation, and a good thorough review by someone.

Chairman NUNN. Would it surprise you to know that the FBI sometimes is surprised when they send a raw report with all sorts of allegations in it, and nobody ever says anything else about it to them, and it just breezes on through? They say, what happened? They do not have any way of doing anything except sending the report in.

Ms. BUCK. Well, I think that is of great concern.

Chairman **Nunn**. Well, it is. I think we have got to readdress the situation. I think we have to take a look too, because for instance in our committee, we have the key counsel on both sides working with Senator Warner and me reviewing the financial information like you do, for a potential conflict.

Of course, we work very closely with you. We rely primarily on your judgment, but we do a review. Then the FBI report is so restricted that the two staff people who review that financial information, which is also private, never see the FBI report. It is given to the chairman and ranking member, under the new procedure—it used to be just the chairman—and that individual, as a Senator, has never seen the financial information.

The same people that review the financial information in any kind of logical investigation, have to also be aware of the FBI report I think, whether it is in the Department of Defense or whether it is in this committee, otherwise you just do not have a check and balance in the system.

But I will get you thinking about that. I would like for the Secretary to think about it too, because it is really being done on your behalf.

Mr. Secretary, let me shift to another area of this. There are all sorts of concerns in the country and on Capitol Hill about the proliferation of so-called black programs. By that I mean the most secret programs we have.

Have you reviewed this series of allegations in the procurement business that has come out in recent weeks with a view in mind to see whether the black programs are more susceptible to the allegations of fraud than the open programs? Do you have any such review underway? Or indications of whether black programs are more trouble?

Secretary **Carlucci**. We have no indications at this point that there are black programs that have been involved. Now, only one of the affidavits has been unsealed. So we really have no choice but to await the unsealing of the other affidavits.

Chairman **Nunn**. So that is an open question?

Secretary **Carlucci**. That is an open question.

Chairman **Nunn**. We do not know one way or the other?

Secretary **Carlucci**. No, we do not know one way or the other.

Chairman **Nunn**. Do you have any kind of review underway, Dr. Costello, as to whether we have too many black programs in the Department of Defense and whether the classification of black programs is, in many cases, instead of being so much driven by secrecy, is driven by an effort to avoid the normal bureaucratic rigamarole? Do you have any check on that?

Dr. **Costello**. Since I am responsible directly for that, yes, we review it on a consistent basis. I have asked everybody if black programs are that much easier, why not use all those regulations on the other programs, we run? So it may be a two way street.

We have looked carefully. I personally reviewed all the programs with General Glenn, the Director for Special Programs on the acquisition side, who reports directly to me. There has been some concern that maybe we have abused the privilege of classification for other than the technical aspects of it, and I see no evidence of that at all. I see no evidence of that at all.

Chairman NUNN. You have a constant ongoing review on that?

Dr. COSTELLO. We actually have probably a more rigorous review of black programs than we do of equivalent size white programs.

Chairman NUNN. Would you keep us informed as these allegation become, if they do, indictments, and as the indictments produce evidence as to whether the black programs are indeed more susceptible?

Dr. COSTELLO. We absolutely will. We would be very concerned about any activity that would lead us to that conclusion.

Chairman NUNN. Senator Warner.

Senator WARNER. Thank you. Ms. Buck, I certainly want to say that those of us here in the Senate admire the professionalism with which you have addressed these issues and the manner in which you have dealt with the sensitivity of the issues. We commend you.

Mr. Secretary, in 1986 the Congress passed legislation to regulate the revolving door between the Department of Defense and the private sector. This law took effect on April 16, 1987 after some of the individuals reportedly under investigation had already left the Department.

Have you reviewed this legislation and the implementation by the Department of Defense to assess whether it is sufficiently effective to prevent impropriety, or the perception of impropriety, by former officers of the military and employees of the Department?

Secretary CARLUCCI. That is one of the issues that is being addressed by the task force cochaired by Ms. Buck and Dr. Costello.

Senator WARNER. So at this time we will just await the report of the task force and your recommendation?

Secretary CARLUCCI. Yes, sir.

Senator WARNER. With respect to the issue of access to source selection sensitive information, it seems to us that we have a different problem than that involved with security of classified data.

In the case of classified data, a degree of compartmentalization is clearly desirable. In the source selection process, however, it seems to be more advantageous to have a contractor's proposal and the evaluation criteria reviewed by many people with expertise in different areas.

How do we protect the contractor's proprietary data under these circumstances?

Secretary CARLUCCI. We, of course, have standards of ethics that are used by the source selection authority, by the different advisory panels, and we expect people to adhere to these codes of ethics. They are all spelled out in the defense acquisition regulations in quite some detail.

So regulations a-plenty there are. Once again, the failing may be a human failing here.

Senator WARNER. The source selection procedures in the Department of Defense have been explicitly designed to reduce the ability of any individual within the system to decisively influence the outcome. The duties of the various source selection boards are separate and there are multiple layers of review for each decision, as you pointed out this morning.

What in your view, are the vulnerabilities of this system to undue influence by individuals?

Secretary **Carlucci**. If the question pertains to the source selection advisory board, I do not know that that particular vehicle is in itself vulnerable. If the question pertains to the overall process——

Senator **Warner**. The overall process.

Secretary **Carlucci**. Then I quite agree with the implication in the question. The overall process has too many decision points in it, and each decision point is a point of vulnerability.

I described it as venal vulnerability, in some cases, where people who have a corrupt tendency can avail themselves of the opportunity. So I think we have to look at the process. There have been a couple of the members who have commented on best and final offer and that is one that ought to come under scrutiny.

I would urge the Congress to pursue the recommendations that have been made by this committee, in terms of having the funding correspond with the milestone process, in terms of multi-year contracts, in terms of biennial budgeting, multi-year budgeting, those are all steps in the right direction to reduce vulnerability of the process.

Senator **Warner**. I thank the Secretary.

Senator **Levin**. Senator Bingaman.

Senator **Bingaman**. Thank you, Mr. Chairman. Mr. Secretary, Senator Levin was asking about the consultants who work for the Department of Defense and the requirements we have there. The other side of it, of course, and the one that seems to be more directly involved in, at least the news accounts of this current scandal, are the consultants that work for the companies, for defense contractors.

And you said, in one of your comments there, we have no real control over those consultants. I would like to just explore that a little bit.

Does the Department of Defense have the ability to cancel a contract with a defense contractor because of illegal acts by a consultant on contract to that defense contractor?

Secretary **Carlucci**. I would think we do. I will defer to counsel in a minute on that. I did not mean to imply that we have no real control, while I did say that. On reflection, we do. We reimburse for legitimate consulting activities, so we have some standards out there for consultants.

What I really should have said is that we do not keep track of consultants hired by contractors. Maybe that is an issue we ought to address, although I do not know how much bureaucracy that would take, probably quite a bit.

Right now, many of the contractors are reviewing their consultant activities. In fact, I dare say most of them. And we are looking at ways that we might deal with this issue, but we have not come to any conclusions.

But let me ask Ms. Buck to address the question of termination for activities of consultants.

Ms. **Buck**. First of all, even without illegal conduct, we have the opportunity to terminate for the convenience of the Government, so we do not need illegal conduct. We do not need to have any finding of criminal conduct beyond a reasonable doubt for us to decide to take action if we think that it is in the public interest to do so.

So I think that we have very solid legal authority to take action here.

Going beyond that, of course, I do think that you are getting into one of the specific issues that is raised in the fraud investigation, and that is something on which we will be focusing. I would envision that that will be a specific part of the report that we produce out of the joint task force.

Senator **BINGAMAN**. If you terminate a contract for convenience, the Government has to pay, as I understand it.

Ms. **BUCK**. The Government pays certain costs associated with the contract, depending on where the contract is——

Senator **BINGAMAN**. But there is not a termination clause that says you can terminate for convenience if you are willing to pay what you are contracted to pay?

Ms. **BUCK**. I think you are also talking about a situation in which we do not want to pay. Is that what you are getting at? If we think there has been fraudulent activity, then we are not going to probably be looking just to terminate for convenience.

It is going to depend on the evidence we have, quite frankly, and whether it is attributable to the company and attributable to the particular contract. Then I think if all of those facts are true, we would be looking at other possible remedies, such as a rescission of the contract, and possibly a recoupment of profits. I think we will be looking at a variety of remedies.

Senator **BINGAMAN**. The point I am trying to get at is, it seems to me when you get down to the real core issue here, your focus has to be on how do you ensure that the folks working for the Department of Defense are in fact loyal to the Department of Defense, not involved in conflicts of interest that keep them from being appropriately loyal in their actions. Then in the case of contractors, you have got to ensure that there is accountability. So that if you have got a contract with a defense contractor, you have got to ensure that you can impose penalties and sanctions and perhaps termination of contracts on that defense contractor, if the actions of a consultant to that defense contractor are inappropriate.

That is what I am just trying to get at, as to whether you feel that you, either by virtue of the contract you have with the defense contractor, do you have that authority to terminate the contract without paying, or do you think that we need statutes to permit us, or to permit you, to impose penalties or sanctions on a defense contractor, if the actions of the consultant are inappropriate? That is what I am getting at.

We had testimony in the Governmental Affairs Committee the other day saying that defense contractors can avoid legal liability by virtue of having a contract with a consulting firm and if the consulting firm does something inappropriate, it cannot be—the defense contractor cannot be held accountable for it.

Ms. **BUCK**. I would not agree with that, and I would hate to get into the position here of prejudging all of our remedies.

I would just like to say that we are going to be looking at every possible line of approach here that we might be able to take, and I simply, at this point in time, would not agree with that assumption.

Senator **Bingaman**. Some of the other testimony we had on Friday in the Governmental Affairs Committee was to the effect that there is a major loophole in the revolving door legislation that Congress has passed, in that a person who leaves the Government service and goes to work for a consulting firm, which then does work for a defense contractor, is not subject to the same prohibitions in working for that consulting firm that the person would be if they went to work directly for the defense contractor.

Are you aware of any problem with the revolving door law, in that respect?

Ms. **Buck**. At this point in time, I do not think that that is a problem. I think that we can—we have several different statutes on the books that reach a person who is leaving the Government and tries to go to work for a contractor or something that they were involved in while they were in the Government.

We have laws on the books to protect against that sort of situation. We have a different set of laws that gets at the person who is the contracting officer who has been working with a specific contractor and who wants to turn around and go to work for that contractor. They cannot do it.

We have a whole variety of laws that are set up now. But we are going to specifically look at the conflicts of interest rules and laws that we have on the books, in the course of this fraud investigation.

Right now, I am not in a position to say that we need anything new, but the door is open, I think, to looking at whether or not we need anything new.

Senator **Bingaman**. Thank you. My time is up. Let me just bring to your attention, the testimony we did receive at the Governmental Affairs Committee hearing we had Friday, and ask you folks to look at it in the task force that you have set up, because there were several specific problems alleged in the present law as it reflects to these consultants.

Ms. **Buck**. The Secretary just pointed out that we do currently have 12 different statutes dealing with conflicts of interest. So at this point in time, I think that while we are going to be looking at those issues in the context of our review, I think that we are not in a position to say that it is inadequate.

Senator **Bingaman**. Thank you very much, Mr. Chairman.

Senator **Levin**. Thank you, Senator Bingaman. Let me go back to the question of consultants that we hire directly by the Department of Defense that are under contract.

I am not here talking about the consultants to the companies that obtain information improperly from us, but the consultants to us that we hire. Now, how many of those consultants are special Government employees, roughly? Do you know, Ms. Buck? Would it be most, or less than half, or what?

Ms. **Buck**. I think generally we consider our consultants to be special Government employees. I think that is the general approach, that they would fall within the definition under the law of special Government employee.

Senator **Levin**. So all the action is taken to every contractual consultant, somebody who just signs a contract with his firm for $100,000 to supply us information, we say, routinely, that person——

Ms. Buck. No. Are you talking about the individuals that we bring in as consultants directly to us, or are you talking about our hiring XYZ firm to do a study or something?

Senator Levin. Either way.

Ms. Buck. When we bring in individuals to work for us, they are filling out forms 1555, the conflict of interest forms, and we are looking at their conflicts, and we are treating them, as far as I know, as special Government employees.

With respect to hiring XYZ firm to do a study for us, I do not think that we would be having those individuals filling out conflict of interest forms, unless they are captured under one of the other statutes, if for example, they just left Government service.

Senator Levin. Well, how many consultants are there like that? Thousands? Tens of thousands? Companies? XYZ companies who we hire?

Ms. Buck. To do studies?

Senator Levin. Yes.

Ms. Buck. I do not know how many.

Senator Levin. Give me a rough estimate.

Ms. Buck. I have no idea.

Secretary Carlucci. We can give you a dollar figure.

Senator Levin. Can you give me a rough estimate of the number of companies?

Secretary Carlucci. I would have to submit that for the record.

[The information follows:]

A rough estimate of the number of companies which perform studies for the Department of Defense is 200.

Senator Levin. Could there be thousands of those companies?

Secretary Carlucci. I suppose there could be over a thousand. Some of them are very small companies.

Senator Levin. I understand that. But that is what I want to get to, because this is the loophole that we have identified, that those companies are not required to file disclosure forms, so that when they come in and give you advice, you do not know routinely who their other clients are, where there may be a temptation on their part, or an appearance of a temptation on their part, to let other clients know what they are advising you.

Secretary Carlucci. I will have to submit something for the record on that. My impression was that they do have to.

[The information follows:]

Under the standards of conduct laws, persons hired by the Government are required to be loyal to the Government. They may not have conflicting interests. (See for example, 18 U.S.C. § 208). Individuals serving in temporary or intermittent positions are considered "special Government employees." Although some of their limitations are less strict than those of regular Government employees, they also are required to have no interests that are inconsistent with the duties they perform for the Government. Individuals employed by contractors, rather than by the Government, are a third category. They do not have the obligation to the Government of either regular or special Government employees.

Accordingly, when the Government contracts with business entities for studies or other work, the source of that product is taken into consideration when evaluating the work. The Government's authority to collect personal financial information from its officer and employees has survived challenge. There is reason to doubt that there would be the same success if the Department demanded similar information from individuals employed by contractors.

Senator **Levin**. Well, Ms. Buck just said that they are not special Government employees, and this form is limited to special Government employees.

Secretary **Carlucci**. A firm, as opposed to an individual?

Senator **Levin**. Sure.

Secretary **Carlucci**. We will be glad to look at that.

Senator **Levin**. Do you know whether we have a form 1555 on Melvin Paisley?

Secretary **Carlucci**. He is not a consultant to us.

Senator **Levin**. Well, according to the newspaper accounts, he continued to be a consultant to the Navy.

Dr. **Costello**. His employment was terminated by Secretary Webb.

Senator **Levin**. Yes, but until then, he was a consultant to the Navy.

Secretary **Carlucci**. There may be a form. I assume that if there is, the Justice Department has got it.

Senator **Levin**. That would be something which you could share with this committee.

Ms. **Buck**. If he had been a consultant directly to the Navy, he should have filed a form 1555, and we will be happy to check on that. But in any event, he would also have filed other forms, because of his recent Government service. He filed a form 1787.

Senator **Levin**. I am just talking about that one form.

Ms. **Buck**. We will check on that. But that was terminated, I believe, some time ago.

Senator **Levin**. I understand that. Until it was terminated, he presumably would have had a form 1555 on file?

Ms. **Buck**. I think so.

Senator **Levin**. Would you submit that to the committee?

Ms. **Buck**. Certainly.

Senator **Levin**. And the same with Mark Sanders.

Ms. **Buck**. Yes, sir, we will check on that.

[The information follows:]

The Department of the Navy advised that Navy records indicate that neither individual served as a consultant. The proposed arrangement to have Mr. Paisely serve was rejected before the paperwork was processed. There was no DD Form 1555 filed by either person.

Senator **Levin**. Mr. Secretary, one of the allegations in the current scandal is that the insider information utilization has been going on for a long time. In the one instance cited in the Wall Street Journal, a contractor selection officer for a Navy program was "pushed into retirement" after he was caught providing inside information to one of three competitors on the Aegis cruiser program.

A second selection officer was then assigned to the job, but was then caught doing the same thing with a second company, and was also "edged into retirement." These are reports I am quoting from. According to the Wall Street Journal, a third selection officer awarded the contract to the only remaining competitor which had not seen inside information.

We have the GTE case, where these allegations were made in court, I think in 1983, of significant utilization as a matter of practice and routine, inside the Defense Department.

What was and is your understanding of this? How widespread and commonplace is it? How long has it been going on?

Secretary CARLUCCI. Senator Levin, I honestly cannot answer that question until we have received the information from the prosecutor. The vast majority of DOD employees adhere to the rules and do not divulge this information. And we would not have any access into the community that apparently has engaged in this type of activity.

The prosecutor has said that this is a rather large occurrence, but large by what standard? Until we actually see the affidavits and see the evidence, those are judgments that we just cannot make.

Senator LEVIN. You have no opinion as to how extensive the use of inside information has been, how commonplace?

Secretary CARLUCCI. I have no—well, it depends on what you mean by inside information. Certainly every defense contractor engages in market intelligence. In fact, that is one of the points I tried to make.

Senator LEVIN. I am talking about improper.

Secretary CARLUCCI. Improper information—I would have no grounds for making a judgment on that until I see criminal cases. If anybody lets me know about it, I will certainly take appropriate legal action. Now, I am just not in a position to know.

Senator LEVIN. Well, no one may tell you about it, but there is insight into these in institutions, common understandings, rumors, feelings, beliefs, there are either beliefs or not. We have certain beliefs inside the Senate, as to certain things happening; we may not be able to prove it, but was there and is there a belief inside the Defense Department that the use of improper—that improper use of inside information is relatively commonplace? Did that belief exist within the Department of Defense?

Secretary CARLUCCI. I have heard people say that, but I cannot say that that kind of rumor is widespread. However, I have heard people say just the opposite. I have heard people say that the system is very tight.

Senator LEVIN. So it has not been a commonly held belief?

Secretary CARLUCCI. Not to my knowledge, but Dr. Costello is closer to it than I.

Dr. COSTELLO. I am a relative newcomer. I have been here for almost 2 years now, and I do not see the infrastructure of communicating information that should not be classified or sensitive. I think that the services probably exercise, from my judgment, from what I have seen, at least as careful and probably better control than I was used to in the commercial world.

Senator LEVIN. Thank you, Dr. Costello.

Secretary CARLUCCI. We could be wrong. We could be wrong. When the evidence comes out, we will certainly act on that if that is the case.

Chairman NUNN. Mr. Secretary, let me shift to yet another subject that we have touched on this morning, and that is the General Accounting Office testimony yesterday, that Mr. Bowsner said that he was predicting that the other shoe is going to drop on cost growth and cost overruns. You mentioned that a few mintues ago, and you stated, if I am capturing it correctly, that over the last 2 years the systems acquisition reports—which are in effect a predictor of how costs are coming—that those have been virtually zero in terms of overruns.

That is good news. That is very big, billions and billions of dollars there, when you get into cost overruns. And inflation being down, of course, is one of the principal ingredients, the lack of having an inflationary growth pattern.

But I am very concerned, as the General Accounting Office has expressed, because the SAR reports, if I am correct, and you correct me if I am wrong, are based on the total lifetime expectation of unit cost of a particular weapon system, is that right?

Secretary CARLUCCI. That is my understanding.

Chairman NUNN. So, it is a lifetime cost based on the total cost divided by the number of units. Mr. Costello, how do you determine the number of units that are going to be produced in any given weapon system as a foundation for the SAR report in determining that unit cost?

Dr. COSTELLO. The SAR reports are put together by the Comptroller, and then they can have him report, for the record, exactly the process and the system used.

Secretary CARLUCCI. I assume it is what is in the FYDP.

Chairman NUNN. It is in the 5-year defense plan. Alright, here is the problem. The 5-year defense plan, as you know, has to be pruned back by $200 to $250 billion dollars in order to meet the now President Reagan's budget, is that correct, Mr. Secretary?

Secretary CARLUCCI. Yes; and I am prepared to concede that this is a problem. I indicated to, I guess it was Senator Bingaman, that with declining budgets, we are going to face some pretty hard choices in this area. And there is a danger.

Chairman NUNN. Then what we have now, if I understand it, is systems acquisition reports that do not even come close to reflecting what is going to happen.

Secretary CARLUCCI. Oh, I would not——

Dr. COSTELLO. I would like to answer the question. On all major programs, they are reviewed quarterly, in detail, every single program, for cost, performance, et cetera, by the immediate OSD staff, and me. We have an independent review, and we have charged the functional staff hard to work directly with the program people to ensure that the Service Acquisition Executives are using the same data, and we are tracking that on a quarterly basis.

Chairman NUNN. But here is my point. The SAR is based on a 5-year defense plan that is grossly in excess of President Reagan's own budget projections. The numbers that are divided into the total acquisition cost are based on the procurement numbers in that 5-year defense plan, am I right so far?

Secretary CARLUCCI. Yes, except that that does not mean that because we are going to have to take $250 billion out of that system does not mean that it all comes out of the particular SAR systems. We may be able to protect some of those systems.

Chairman NUNN. But the way you avoid cost overruns appearing in those SAR reports is to inflate the number of units being produced so you have a larger number of units being produced on paper, compared to what really is going to happen.

Secretary CARLUCCI. I would not use the word, inflate, Mr. Chairman. In the M-1 tank we have a total buy, which this committee is aware of, and the SAR would be based on that total buy.

Chairman NUNN. But over a certain time, and if you stretch the time frame by 7 or 8 years, the unit cost goes way up.

Secretary CARLUCCI. That is correct.

Chairman NUNN. I am told on the C-17, I think this year we had six, is that right, in the budget?

Dr. COSTELLO. The first year is six.

Chairman NUNN. What will the next year's be, the likely number.

Dr. COSTELLO. I looked at the numbers yesterday and I am scratching my memory.

Secretary CARLUCCI. Sixteen, I am told, though we are still going through that process.

Chairman NUNN. But I am told that the SAR is pegged at 28. They were going to produce 28 C-17's per year, and so that point is that General Accounting Office is predicting, based on reality, that we are going to have cost overruns. The SAR report, now, is not based on reality. It is based on a 5-year defense plan and a pace of procurement that has no connection with what is going to happen.

Secretary CARLUCCI. Well, that is a bit of an unfair charge, because obviously we have gotten the costs down over the period, and we have done it by inflating the out year numbers. We put into the program structure what we thought was a viable program.

Chairman NUNN. I am really talking about the future. I am not charging any kind of abuse in the past. I am talking about where we are now.

Secretary CARLUCCI. When the budget ramps down, there is absolutely no question that you are going to have a problem with weapons systems and the possibility of cost escalation because it is going to be very hard to keep them at economic rates. I have tried, as you know, I have tried to avoid the stretch outs. We will try, in the future, but I am informed, as we put together the 1990 budget, that is becoming increasingly difficult.

Chairman NUNN. When will you have a new 5-year defense plan?

Secretary CARLUCCI. When we submit the 1990 budget. We are going through that exercise right now.

Chairman NUNN. At that time, will the SAR reports reflect the——

Dr. COSTELLO. They will be redone.

Chairman NUNN. So we will have some real adjustments to make in the SAR report at that time.

Secretary CARLUCCI. Yes, we will.

Chairman NUNN. They really do not tell us much now.

Dr. COSTELLO. We are in a time of change.

Secretary CARLUCCI. I concede that point. They tell us historically that we have had a good record in bringing the costs down, but they are not I quite agree, they are not a good predictor of the future, because they are based on certain budget assumptions that are not realistic.

Chairman NUNN. Mr. Secretary, if we are going to get stability in defense spending, which I share with you as a major goal, and I also think the ups and downs, the roller-coaster 10 percent growth

1 year, 12 percent the next, 2 percent the next, 2 percent minus the next, that roller-coaster is probably the worst way we waste money in the Defense Department, would you say?

Secretary Carlucci. I quite agree.

Chairman Nunn. Probably more than any conceivable amount of fraud could be, if you add it up.

Secretary Carlucci. You have probably seen my chart, where I show that if we had had just zero real growth, since, 1970, we would be better off than we are today with the ups and downs.

Chairman Nunn. Well, I hope you will perhaps influence this President to make a proposal with his next budget, which he will make before he goes out of office, that would at least, whoever is elected President, would set up an early procedure in the next administration to identify four or five numbers for at least a 2-year period.

We have passed all the Appropriation Committee bills, everything has passed the House of Representatives, we now have every appropriation bill out of the Senate Appropriations Committee. We have a chance, unless we get into a filibuster on something unforeseen, to finish all the appropriations bills by the beginning of the fiscal year.

Now, that is not a coincidence. The reason it has been done is because we had an agreement between the Congress, the Republicans and Democrats and the President on four of five numbers.

One number, the total expenditures anticipated over a 2-year period. Next number, total revenues over a 2-year period. The next number, the total for entitlements within the expenditures. The next number is the total for discretionary spending. Then the next number, key number for all those of us in Defense, is the Defense number.

You do not have to have a whole budget agreement on everything; but if the President and the Congress can get together on five numbers at the beginning of the process, then this system can work much much better, and we have a chance of coming out of it with some stability in defense.

So I would hope that you would take that into account in deliberations on the defense number. There is no way that we can have stability in defense spending without those other four numbers.

Secretary Carlucci. I think that is a fair point.

Chairman Nunn. That is what this administration has been striving for, predictability in defense without coming to an agreement on the other numbers. Now Congress and the administration have to work together in that respect, but I urge you to take that into account, because that is the way that we can get some predictability in the system.

I understand you have a time problem. I know that my time has expired. Senator Levin.

Senator Levin. Just a few more questions, Mr. Chairman. Back to this question of inside information. Mr. Secretary, you were making reference to the proper use of information, and you started to describe the market intelligence efforts that some defense contractors make.

What is proper in terms of obtaining information relative to a contract that you would call market intelligence properly used?

Secretary **Carlucci**. Getting information, say, from the budget on what the proposals for the system are, what the funding profile is, trying to find out by talking to people in the executive branch and Members of Congress.

Senator **Levin**. How about from the contracting officer?

Secretary **Carlucci**. From the contracting officer, there are conferences that are held with bidders, and I would say that, in fact, I have sent a memo out saying that any ex parte contact is not appropriate.

Senator **Levin**. You are not suggesting that a contracting officer could supply one company anything that is not——

Secretary **Carlucci**. Absolutely not.

Senator **Levin**. Again, relative to inside information, we were talking about rumors and understandings in the Defense Department before, relative to the use of it.

We had a situation, the *GTE* and *Zettl* case, in the Eastern District of Virginia, where GTE has actually pled guilty to improper utilization of inside information, which was obtained, they admit, by Mr. Zettl, who has been indicted but has not yet been tried, as I understand it.

Do we know where that inside information came from?

Secretary **Carlucci**. I am not familiar with that case.

Senator **Levin**. What effort was made to find out who, in the Defense Department, provided that inside information that GTE pled guilty to. Could someone tell us that?

Ms. **Buck**. That case has not come to trial yet, so it would be inappropriate—GTE pled guilty and I just do not have the names of all the individuals who were involved in that case, and since it is tied in——

Senator **Levin**. I do not want the names. I am interested in knowing—do we know who, inside the Defense Department, provided that information that GTE had pled guilty for using?

Ms. **Buck**. I do not, but we will try to get that for the record for you.

[The information follows:]

CONGRESSIONAL TESTIMONY-DEFENSE ACQUISITION PROCESS

We do not know who, inside the Defense Department, may have provided the information that GTE pled guilty to using. However, that line of inquiry is still an open matter in the Zettl case.

Senator **Levin**. Let us know, if you would. If we do know who it is, what action was taken against that person? If we do not know who that person is, what efforts were made to locate that person or persons?

Mr. Secretary, you made reference today to preparing a protocol to help you piece through the question of how to handle tainted contracts. Yesterday you announced that some of the companies that had previously been suspended were now back, that you had unsuspended them. You had lifted the suspension.

Secretary **Carlucci**. It was a feeeze on payments.

Senator **Levin**. That is correct. You had unfrozen their payments. Does that mean that you have satisfied yourself that there is no taint on those contracts? Or does that mean that those contracts will be handled pursuant to the protocol which you are now working on?

Secretary CARLUCCI. The former, but on a provisional basis. This has been inaccurately described in the press, by the way. We put a freeze on, for the purpose of allowing us to review the contracts in the light of existing information.

We have done that. We have gone through the contracts and we can find nothing in existing information to indicate that the contracts are tainted.

Therefore, we have lifted the freeze, which was always our intent. But, in doing so, we have sent out a warning which says that this does not mean that if there is further information that comes to light, we will now once again review this contract and, if it is tainted, take appropriate action.

Senator LEVIN. My last question relates to that Office of Government Ethics review of the Navy in June of 1986 which I made reference to before, and which you will give us a response to. Now, the Office of Government Ethics is in the executive branch, so this is not a legislative or judicial finding. This is right inside the executive branch.

The review says that the Navy and the DOD continue to be plagued by the spectre of post-employment revolving door, whereby personnel leaving DOD go to work for contractors, and vice versa, are engaged in some type of wrong-doing. And the OGE put a lot of blame on the Navy's "inability to vigorously pursue such violations, the lack of sensitivity and awareness concerning the post-employment restrictions, and the lack of an effective system for preventing violations."

I have asked you this question; let me ask your two colleagues here. Do either of the two of you know what actions the Navy or the Department of Defense took in response to the Office of Government Ethics criticisms in 2 years?

Ms. BUCK. I do not have that information with me.

Dr. COSTELLO. Neither do I, Senator.

Ms. BUCK. We can get a specific response for you on that, and I think we would like to do that.

[The information follows:]

The Office of Government Ethics (OGE) performs a valuable service when it audits the Standards of Conduct programs of the components of the Department of Defense. The review reported by the Director of the Office of Government Ethics was very helpful. Although in his June 9, 1986 report he concluded that the Navy had "a sound ethics program," he added that there were several areas where improvements were needed. Those improvements are nearly completed.

These are the highlights of the steps that have been taken:

1. On several matters the Navy regulations needed updating and more detailed guidance. The completely revised DoD Standards of Conduct Directive (DoDD 5500.7) was issued May 6, 1987. The Navy's draft implementation of that Directive, which includes the OGE suggestions, presently is receiving its final coordination and will be published very soon.

2. OGE representatives met with Navy ethics officials May 26, 1987 and had a number of follow-up conversations described in OGE memoranda of May 29, 1987, and June 19, 1987. These generally expressed satisfaction with the Navy's remedial actions, noting specifically the following:

a. Flaws in the financial disclosure report tracking system were corrected.

b. Technical problems in completion and review of financial disclosure reports were corrected by detailed instructions to the reviewing officials from the Assistant General Counsel (Ethics).

c. More current lists of Department of the Navy contractors were made available to reviewing officers.

d. Improved educational, training, and counseling procedures have been put in place.

The Navy has followed both the letter and the spirit of the OGE suggestions.

Senator LEVIN. So that you know which report we are referring to, it is the June 9, 1986 report to the Navy from the Office of Government Ethics. Thank you.

Chairman NUNN. Mr. Secretary, I know you are hosting a luncheon, and we promised to get you out of here by 12 o'clock. We have missed it by 15 minutes. We hope you make it, and we thank you for being here. We are going to continue to give oversight to this matter, and we are going to continue to work with you. We thank you and Ms. Buck and Dr. Costello for being here today.

Secretary CARLUCCI. Thank you, Mr. Chairman.

[Questions for the hearing record with answers supplied follow:]

QUESTIONS SUBMITTED BY SENATOR SAM NUNN

COMPETITIVE NEGOTIATION

Senator NUNN. Please describe how the source selection process works in a competitive negotiation, with a particular emphasis on the points in the process that are especially vulnerable to fraud?

Secretary CARLUCCI. As indicated earlier, there are critical review points in the Defense Acquisition Process and in the Defense Budgeting and Legislative Oversight Process. The Defense Acquisition Process can take from 10 to 25 years to encompass Milestones 0 through V. Typically, separate contracts are negotiated in each phase. Budgeting and Legislative Oversight occurs annually, even with a biennial budget. The source selection process begins with a definition of the requirement to meet a mission need. At each Milestone, the requirement is defined for the next phase. The requirements document is the basis for the statement of work and specifications incorporated in a solicitation. The source selection plan enumerates the evaluation criteria for offers in response to the solicitation. Offers are evaluated against the criteria and areas for clarification or negotiation are identified for those offers which are considered to be in the competitive range. If negotitions are conducted, best and final offers are solicited and evaluated. The source selection decision is made by the Source Selection Authority. It is important to note that the processes involved in the acquisition of defense systems contain numerous opportunities for intervention at the points where plans and other documents are formulated and where program decisions are made.

EFFECT ON NATIONAL DEFENSE

Senator NUNN. The allegations that have been made public involve abuse of the source selection process in terms of improper disclosure of information, collusive bidding, and alteration of specifications or evaluation criteria to favor a particular offeror. Please describe how each of these abuses can affect our national defense in terms of price, capability of such systems to meet a valid national defense requirement, and the quality and reliability of equipment we provide to our men and women in uniform?

Secretary CARLUCCI. Improper disclosure of information, collusive bidding, and alteration of specifications or evaluation criteria to favor a particular offeror can result in prices that are not fair and reasonable, system capabilities that do not meet requirements, and equipment that does meet quality and reliability requirements. To the extent that abuse exists in the source selection process and is not discovered before award, it can result in a detrimental effect on the national security. How each actual abuse affects security can be determined only by an assessment of the individual case.

DISCLOSURE OF SOURCE SELECTION INFORMATION

Senator NUNN. The public information on allegations now under investigation has focused on disclosure of information during the source selection process. In the conduct of competitive negotiations, discussions between the government and potential offerors are an integral part of the process. What criteria has the Department of Defense developed for distinguishing between the types of source selection information that should be disclosed and the information that should be secured? How much is this left primarily to the discretion of individual contracting officers?

Secretary CARLUCCI. The objective of the source selection process is to select contractors that can best meet the Department's needs. To do so, the process is designed to ensure the impartial, equitable, and comprehensive evaluation of offerors' proposals. Public information or allegations now under investigation have indicated that some individuals not involved in the source selection process may have succeeded in passing information outside of the process. Public information also indicates that, in a few cases, persons actually involved in the source selection process may have violated the rules for fairness in written and oral discussions outlined in the Federal Acquisition Regulation and the Department's Directive on source selection. Contracting officers and other persons involved in source selection have guidelines on the effectiveness and integrity of a source selection in the form of Standards of Conduct, the Source Selection Plan, Departmental Directives, and the Federal Acquisition Regulation. Compliance is mandatory. Guidance is specific on fairness in the conduct of discussions to preclude technical leveling, technical transfusion, and auctioning techniques. Public information on allegations now under investigation suggest that alleged misconduct is not a question of ignorance of the rules or inadequacy of the rules, but rather a deliberate attempt to circumvent the rules. It appears that charges will be brought against alleged perpetrators.

Senator NUNN. Should consideration be given to promoting greater sharing of information during competitive negotiations, with prohibitions on disclosure applying only to proprietary data and cost proposals?

Secretary CARLUCCI. This is not a question of greater or lesser sharing of information. The basic consideration of fairness in competitive negotiations demands that all offerors be provided the same government information and that contractor technical and cost information submitted in confidence for purposes of proposal evaluation be protected from disclosure. Typically, the latter information is of the kind that normally would not be disclosed in a commercial contracting situation. As to information supplied by the government, it is normally a practice to disclose all technical information pertinent to a requirement that the government owns so that offerors can be as informed as possible when they prepare their proposals. This normally includes classified information.

FRAUD REMEDIES AVAILABLE TO THE GOVERNMENT

Senator NUNN. Please describe the remedies that are available to the government in the event of fraud. In your discussion, please distinguish between those remedies that involve termination of the contract and those remedies that can be taken when the government decides that it is in the national interest for the contract to be completed.

Secretary CARLUCCI. Suspension or debarment are used when it is necessary to protect the government's interest in dealing only with reputable, responsible contractors. Suspension or debarment may not be used for purposes of punishment. The Government may terminate a contract for default (e.g. when a contractor gives a gratuity to a government official to obtain a contract or favorable treatment under a contract). The government may seek damages under the contract, including exemplary damages of not less than 3 nor more than 10 times the cost incurred by the contractor in giving the gratuity. Additionally, the Government may declare void and rescind any contract in relation to which there has been final conviction for bribery or conflict of interest. In this case, the Government is entitled to recover the amount expended under the contract in addition to any penalties prescribed by law or in the contract. In addition, we have put into effect a procedure whereby we will be able to recover the amount of any anticipated profit or ten percent of the contract price in the event of fraudulent activities.

FRAUD REMEDIES AVAILABLE TO DISAPPOINTED OFFERORS

Senator NUNN. Please describe the remedies that are available to the disappointed offerors in the event of fraud. In your discussion, please cover the rights, if any, that a disappointed offeror would have against the government, and the impact of any remedies on the performance of the contracts.

Secretary CARLUCCI. Unsuccessful bidders may protest the award if they believe that the government has not followed proper procedures in the contract selection process. If the protest is upheld, the government could be required to cancel or terminate the contract; if it is not, contractors can appeal any adverse decisions to the courts. They can also seek injunctive relief against the award of the contract. In such cases, the supplies or services may not be obtained within the time they are needed. In addition, there may be an increased cost to the government in procuring the items.

CENTRALIZED ACQUISITION AGENCY

Senator **Nunn**. GAO has examined the concept of a centralized acquisition agency. What are the advantages and disadvantages of such a concept, as compared to the present division of responsibilities between OSD and the services?

Secretary **Carlucci**. We strongly support central procurement policy development within the Office of Secretary of Defense. However, we also believe that operational execution of the procurement function must remain within the Military Departments.

Functions such as requirements determinations, (what systems, what capabilities are necessary to overcome specific military problems) and technical engineering support must remain with the procurement function in the Military Departments.

Separation of these functions, could result in procurement actions being taken without the expertise of the military professionals who understand the problems that must be overcome.

We already procure common supplies such as fuel, uniforms and electronic components through a central buying activity—DLA. Other common items such as office furniture and administrative motor vehicles are bought through GSA. However, centralization of the procurement process is not and has not been a guarantee that problems will not occur.

ACADEMIC PREPARATION

Senator **Nunn**. There are relatively few schools of law, business, or public administration that offer degrees in acquisition management or contract law. What, if anything, can the government do to encourage academia to prepare students for careers in government service related to the acquisition process?

Secretary **Carlucci**. We have been working to increase the professionalism of the acquisition workforce for several years with many concrete accomplishments in this area, including: (a) establishing experience and training requirements for military and civilian acquisition personnel; (b) establishing an improved training structure overseen by the Defense Systems Management College (DSMC); and, (c) working with the Office of Personnel Management to implement the Packard recommendation of requiring 24 semester hours of business courses for entry into the contracting field.

One of the key missions of DSMC in its expanded acquisition training role is to work with the Federal Acquisition Institute (FAI) to encourage more and better acquisition courses. The FAI has been working within its mandate to encourage acquisition training in colleges and universities for government in general. DSMC will help ensure that defense acquisition needs are appropriately represented.

NEED FOR PRIOR ACQUISITION EXPERIENCE

Senator **Nunn**. Should the key acquisition positions in the Department of Defense, such as the Under Secretary for Acquisition, the Service Acquisition Executives, and the functional Assistant Secretaries be filled with persons who receive "on-the-job" training in the government's acquisition process, or are these jobs in which persons should have demonstrated relevant experience in government and industry?

Secretary **Carlucci**. In describing the senior acquisition positions in the Department of Defense, the Packard Commission said that these positions should be filled by people with extensive experience in acquisition. Public Law also requires that the Under Secretary be appointed from among persons with an extensive management background. Extensive experience both in government, and more importantly, in the private sector are essential prerequisites for filling these important positions.

QUALIFICATIONS FOR SENIOR ACQUISITION EXECUTIVES

Senator **Nunn**. What advice would you give the next President in terms of the qualifications that should be established for selection of persons to serve as the Under Secretary for Acquisition and as the Service Acquisition Executives?

Secretary **Carlucci**. Obviously, the next President and Secretary of Defense must have personal confidence in whomever they select. However, I would recommend that the next President heed the advice of the Packard Commission and appoint persons with extensive acquisition experience.

DUPLICATIVE OVERSIGHT

Senator **Nunn**. You have stressed the importance of vigilant oversight to assure that industry institutes needed internal control measures. At the same time observers, including the DoD Inspector General, have noted that the Department's efforts are plagued by unnecessary, duplicative oversight activities. What steps can the Department take to ensure that its oversight resources are used efficiently and not squandered on repetitive, duplicative reviews?

Secretary **Carlucci**. The Defense Acquisition Improvement Act of 1986 assigned to the Under Secretary of Defense for Acquisition the responsibility for prescribing "policies to ensure that audit and oversight of contractor activities are coordinated and carried out in a manner to prevent duplication by different elements of the Department." The attached report highlights the actions taken by the Department of Defense to reduce duplicative and excessive oversight of defense contractors.

Attachment.

The Under Secretary of Defense,
Acquisition (P&L/P),
Washington, DC, June 27, 1988.

Hon. Sam Nunn,
Chairman, Committee on Armed Services, United States Senate, Washington, DC.

Dear Mr. Chairman: I am pleased to report to you on actions taken by the Department of Defense to reduce duplicative and excessive oversight of defense contractors. This report was requested during my confirmation hearing for the position of Under Secretary of Defense for Acquisition before the Senate Armed Services Committee.

The Defense Acquisition Improvement Act of 1986 assigned to the Under Secretary of Defense for Acquisition the responsibility for prescribing "policies to ensure that audit and oversight of contractor activities are coordinated and carried out in a manner to prevent duplication by different elements of the Department." The Act further required that this responsibility be carried out in consultation with the Inspector General of the Department of Defense.

The Inspector General, Ms. June Gibbs Brown, and I are committed to reducing duplicative and excessive oversight. We will continue to work together until we are satisfied that meaningful improvements have been made.

An identical letter has been sent to the Chairman of the House Armed Services Committee.

Sincerely,

R.B. Costello.

Enclosure.

The Under Secretary of Defense,
Acquisition (P&L/P),
Washington, DC, June 27, 1988.

Hon. Les Aspin,
Chairman, Committee on Armed Services, House of Representatives, Washington, DC.

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The Inspector General, Ms. June Gibbs Brown, and I are committed to reducing duplicative and excessive oversight. We will continue to work together until we are satisfied that meaningful improvements have been made.

An identical letter has been sent to the Chairman of the Senate Armed Services Committee.

Sincerely,

R.B. COSTELLO.

Enclosure.

REPORT ON THE REDUCTION OF DUPLICATIVE AND EXCESSIVE OVERSIGHT—BACKGROUND

As part of the Packard Commission's study of the issues surrounding defense management and organization, a review of government auditing and oversight of defense contractors was performed by Arthur Andersen & Co., a certified public accounting firm. The principal problems identified by Arthur Andersen & Co. were: a pervasive lack of coordination among DoD organizations, an indiscriminate approach by DoD organizations in performing audit and oversight, and eroding authority of contracting officers. They concluded that duplication in the oversight process is extensive, and that changes are required to enhance efficiency and reduce costs to both contractors and the government. Arthur Andersen & Co. recommended that the authority of the contracting officer be reaffirmed, that respective audit and oversight responsibilities be reevaluated, that day-to-day working relationships be improved, and that regulatory principles that promote efficiency be followed.

In addition, the Packard Commission recommended that the Under Secretary of Defense for Acquisition (USD(A)): oversee DoD-wide establishment of contract audit policy, particularly policy for audits conducted in support of procurement and contract administration; supervise establishment of policy for all DoD oversight of defense contractors, including oversight performed by procurement and contract management organizations, except for criminal investigations and DoD internal audits; and recognize established General Accounting Office (GAO) and professional auditing standards. They further recommended that, in order to optimize the use of available oversight resources by eliminating undesirable duplication of official effort, contract audit policy should be designed to: delineate clearly respective responsibilities and jurisdictions of DoD oversight organizations; develop guidelines and mechanisms for DoD oversight organizations to share contractor data and otherwise to rely more extensively upon each other's work; and improve audit strategies for the conduct, scope, and frequency of contract auditing. These strategies should reflect due consideration for contractors' past performance, the proven effectiveness of their internal control systems, the results of prior and ongoing reviews conducted by DoD organizations and by contractors themselves, and relative costs and benefits.

As part of the fiscal year 1987 Defense Authorization Act, the USD(A) was directed to prescribe policies to ensure that audit and oversight of contractor activities are coordinated and carried out in a manner to prevent duplication by different elements of the Department. The USD(A) must consult with the Inspector General (IG) in carrying out this function.

Additionally, the Senate Armed Services Committee, in its report on S. 1174, the fiscal year 1988 Defense authorization bill, stated that the USD(A) should consider the establishment of a formal review and clearance mechanism administered by onsite DoD contract administration personnel. This process could be used to review and screen a defense agency's request in order to avoid duplication with prior requests for information or with reviews that are underway or have been recently completed. Conference report language which was issued related to the fiscal year 1988 Defense Authorization Act concurred in the desirability of such a mechanism, and directed that any mechanism adopted to minimize unnecessary duplication provide that contract administration personnel not deny access to contractors' records when the Comptroller General or the DoD IG determines that such records are required to fulfill their statutory responsibilities, or when such records are required by the Defense Contract Audit Agency (DCAA) to comply with established government auditing standards.

ACTIONS TAKEN TO REDUCE DUPLICATIVE AND EXCESSIVE OVERSIGHT

Authority of Contracting Officers

To eliminate the perception that contracting officers are not the final decision-making authority with respect to contractual matters, the Department redefined the respective roles of the contracting officer and the contract auditor through a February 12, 1988 revision to DoD Directive 7640.2, Policy for Followup on Contract Audit Reports. The Directive now recognizes "the independent, decision-making role of the contracting officer and the financial advisory role of the contract auditor." The oversight role that was assigned to auditors has been eliminated, and the designated independent senior acquisition official (who served as advisor to the contracting officer on audit report recommendations that the contracting officer did not agree with) has been replaced by the normal management review process. Additionally, the dollar thresholds at which significant postaward audits must be reported to top acquisition managers and to the IG for reporting to Congress were raised to $100,000.

These revisions help to restore the authority of contracting officers while still providing a viable contract audit followup program. To the extent that the deterioration of the contracting officer's authority as the government's team leader contributed to the problems of duplication and inefficiency in the oversight process, as alleged in the report issued by Arthur Andersen & Co. for the Packard Commission, the revisions to DoD Directive 7640.2 should help to alleviate the problems.

Additionally, the Department is reconsidering the assignment of the responsibility for determining final indirect cost rates and interim billing rates. This responsibility was previously held by contracting officers, but was transferred to contract auditors in 1985. The assignment of this responsibility to contract auditors is frequently cited as contributing to the eroding authority of contracting officers.

Visits to Contractor Facilities

The Federal Acquisition Regulation was revised to specify that prospective visitors to contractor facilities are to provide advance information concerning the visit to on-site government personnel. This notification is for the express purpose of eliminating duplicative reviews, requests, investigations, and audits relating to the contract administration functions which have been delegated to contract administration offices. If the visit will result in reviewing, auditing, or obtaining any information from the contractor related to functions which have been delegated to contract administration offices, on-site government personnel will determine whether information adequate to fulfill the requirement has recently been reviewed by or is already available within the government. If so, the prospective visitor will be referred to the government office where the information is located and the visit will be discouraged.

The Service Acquisition Executives and Directors of Defense Agencies were informed of this new procedure on June 29, 1987, and asked to implement it immediately. Final coverage was published in the Federal Acquisition Regulation on January 11, 1988.

Increase in Thresholds for Preaward Reviews and Audits

Thresholds for preaward reviews and audits of the Department's contracts were raised from $100,000 for firm-fixed-price contracts and $250,000 for fixed-price-incentive contracts to $500,000, and from $500,000 for cost-reimbursement contracts to $1,000,000 on June 4, 1987. Defense contractors have frequently complained that there is duplication in the preaward review area; increasing thresholds reduces the number of reviews and audits that are required to be performed and therefore reduces duplication. At the same time, because of the increased emphasis which the Department is placing on the need for reliable contractor estimating systems and the periodic review of these systems, we believe that proper controls are in place to protect the government's interests.

Requirement to Obtain Contractor Cost or Pricing Data

The Department issued guidance to the Services and Defense Agencies on May 1, 1987, instructing these organizations to refrain from obtaining cost or pricing data when there is a reasonable expectation that adequate price competition will result on a particular proposal. When cost or pricing data are not obtained because adequate price competition has been achieved, there is no requirement to obtain complete preaward reviews and audits. By emphasizing to contracting officers the need to obtain only that data which is necessary for the particular procurement action, unnecessary audit and review activity is minimized.

Contractor Compensation Reviews

As of October 1, 1987, the responsibility for performing contractor compensation reviews was transferred to one agency within the Department to preclude duplicate or overlapping reviews of contractor compensation systems and costs.

ACTIONS IN PROCESS TO REDUCE DUPLICATIVE AND EXCESSIVE OVERSIGHT

Contractor Risk Assessment Guide Program

The Contractor Risk Assessment Guide (CRAG) Program is a recent initiative designed to encourage contractor self-governance, motivate contractors to develop more effective internal control systems, and improve the effectiveness and efficiency of the Department's oversight efforts. The CRAG lists well-defined internal control systems objectives for contractor indirect cost submissions, labor charging systems, material management and accounting systems, estimating systems, and purchasing systems. If a contractor can demonstrate that his internal control system meets the stated objectives in one or more of these areas, audit and oversight in the area(s) will be reduced. Reliance on the integrity of the contractor's internal control system, rather than on detailed transaction audits, results in more efficient use of the Department's resources and contributes to a less adversarial relationship between the Department and industry. Participation by contractors in the CRAG program will be on a voluntary basis.

The Secretary of Defense has recently furnished a copy of the draft guide to 100 of the largest defense contractors, soliciting their comments and support. Ultimately, the Department must retain the responsibility for deciding how much audit and oversight coverage is sufficient to protect the public interest. However, we believe that we can work cooperatively with industry to develop a meaningful CRAG program which is mutually beneficial.

Coordination of the Audit and Review Function

Audit and oversight review policies and procedures are frequently issued by organizations responsible for procurement, contract management, contract administration, and contract audit. There is currently no requirement for centralized review of these policies and procedures to ensure that they are tailored to eliminate the potential for duplication or overlap, and that responsibilities and jurisdictions are clearly assigned to the most appropriate organizations.

A policy letter will be issued requiring a review of all new policies and procedures which impose additional audit of oversight review requirements on contractors. This review will be performed by the offices of the USD(A), the IG, and the Assistant Secretary of Defense (Comptroller) (ASD(C)) to ensure that: a need exists for the type of review being proposed; potential duplication and overlap with other reviews is minimized; the most appropriate organization is assigned the responsibility for performing the review; mandatory professional standards (such as the auditing standards issued by the GAO) are considered; and the cost to both the government and the contractor for performing the review is considered in light of the potential benefits to be achieved.

This requirement minimizes the potential for duplication or overlap in future policies and procedures.

Contractor Purchasing System Reviews

Contractor purchasing system reviews must be conducted by the cognizant contract administration office at least every three years for contractors whose sales to the government are expected to exceed $10 million during the next 12 months. In the period between these reviews, administrative contracting officers (ACOs) periodically test the purchasing system to ensure that the contractor is effectively managing its purchasing program. The ACO makes an annual determination to continue approval or to withdraw approval of the contractor's system. The auditor also performs comprehensive reviews of the contractor's subcontract management program, which is part of the purchasing system. Outside organizations or teams may also review the purchasing system.

Since acquisition regulations assign to the ACO the authority to review contractor purchasing systems, other organizations should not conduct separate reviews. Other organizations may participate in the review conducted by the ACO, or may recommend that an additional review be performed if they believe that a problem exists. If the ACO determines that an additional review is necessary, it should be performed as part of the an ACO-initiated special review.

A working group is currently rewriting the contractor purchasing system review guide and related regulations. The working group has been instructed to incorporate this policy into the guide and regulations.

Coordination Among DOD Internal Auditor Organizations, DCAA, and GAO

The Department should strengthen its audit policy so that internal audit and review organizations are required to utilize the services of the DCAA auditors whenever a review of contractor records is necessary. Internal auditors should find it necessary to review contractor records on an exception basis only. These procedures will prevent situations where, for example, two separate organizations perform effective pricing reviews of the same contract, including separate review of contractor records.

The IG's office is currently revising the necessary policy directives to allow their auditors to place more reliance on DCAA for the review of contractor records. The GAO will be asked to execute a memorandum of understanding which states that they will rely on DCAA to review contractor records whenever possible.

Spare Parts Pricing

The Department has paid increased attention to the area of spare parts pricing since 1983 when allegations of overpricing surfaced. Significant changes were made to the management of the Department's spare parts mission as a result. A rigorous approach was adopted for analyzing contractors' spare parts proposals so that an in-depth evaluation is now required to ensure line item price integrity. DCAA has recently agreed to report audit findings on a line item basis, which serves to eliminate the need for any additional analysis of contractor records by contract administration or procurement personnel.

A policy letter will be issued to procurement and contract administration activities informing them of the need to specifically request line item reporting by the auditor for spare parts pricing proposals.

Additionally, the Department will periodically review the necessity for such in-depth analysis of spare parts proposals to determine if improvements in the pricing of spare parts are sufficient to justify reduced analysis.

Should Cost Reviews

Should cost reviews are specialized forms of cost analysis for individual contract proposals or for overhead forward pricing. A should cost review is performed by an integrated team which evaluates a contractor's proposal on a fully coordinated basis to identify uneconomical and inefficient practices in the contractor's management and operations. The resulting analyses provide the basis for a sound government negotiating position and ultimately result in achievement of more efficient and economical contractor operations.

The decision to conduct a should cost review must be made as early as possible in order to preclude duplication of review and audit effort. Preplanning with the resident contract administration and audit offices is necessary to reduce potential duplication. Information already furnished to the government should be used to the maximum extend possible, and all additional data requested from the contractor must be closely monitored and shared by team members during the review to preclude duplicate requests for contractor data.

A policy letter will be issued to the Services and Defense Agencies emphasizing the importance of these procedures.

Technical Reviews

Policy guidance will be issued to require auditors to rely on the administrative contracting officer for any technical analyses which are needed. Policy letters will also be issued to contract administration organizations instructing them to be fully responsive to these auditor requests.

Program Office Travel to Contractor Facilities

Based upon a review of contractor visitor logs, it appears that the majority of government visitors were personnel from program offices. In some cases, the number of visitors and the frequency of visits may be excessive.

A letter will be issued to the Service Acquisition Executives requesting that they advise program managers to carefully scrutinize travel requirements. The purpose of the visit, size of the team, and frequency of reviews should be considered.

Review of Statutory/Regulatory Requirements

The Logistics Management Institute is analyzing more than 50 oversight requirements which are imposed on contractors by statute or regulation. They are looking particularly at how reviews can be combined or review thresholds raised in order to eliminate excessive or duplicative oversight.

Additional Working Group Effort

The joint working group consisting of representatives from the offices of the USD(A), IG, and ASD(C) is currently reviewing additional areas as follows: quality assurance systems reviews, electronic data processing reviews, pension/insurance reviews, contractor operations reviews performed by the Air Force, contractor systems status reviews performed by the Defense Logistics Agency, and operational audits performed by the DCAA. We anticipate additional actions will be taken as recommendations are developed and staffed.

They are also considering recommendations made by the Ad Hoc Industry Advisory Group to the Defense Industry and Technology Subcommittee of the Senate

Armed Services Committee related to government oversight of defense contractors. The recommendations are: (1) All DoD agencies (except for the IG and DCIS) should be required to coordinate an annual plan for audits and inspections to eliminate duplication and to ensure that government resources are used effectively; and (2) All government agencies should have to accept the work product of any other agency which had conducted the same type of review in any given year.

DOD USE OF CONSULTANTS

Senator NUNN. To what degree does the Department rely on consultants to perform core government functions such as establishment of source selection criteria and evaluation of bids?

Secretary CARLUCCI. By directive, Contracted Advisory Assistance Services can be procured only when the service being contracted for is not an organic governmental function that must be performed in-house (DoDD 4205-2, D.5.c.). The establishment of source selection criteria and the evaluation of bids are such government functions. However, because of the technical aspects involved, experts in the form of contractors are sometimes used to provide recommendations and technical assessments to assist us in our decision process. Any contract providing this type of service would, however, be awarded based on no potential conflict of interest with the programs involved.

IMPACT OF LAWS ON WORKFORCE QUALITY

Senator NUNN. What is the impact of revolving door, conflict of interest, and dual compensation laws on the quality of the acquisition workforce?

Secretary CARLUCCI. The problems we face in attracting into government service talented individuals from the private sector would be exacerbated by the imposition of a broad post-government employment bar. The government clearly benefits by attracting persons from industry who have extensive experience, technical expertise or management talent. For example, a scientist who is an expert in underground nuclear tests and is willing to serve the Department for a few years may decline that opportunity if he cannot return to the private sector and work in his field of expertise. It has been our experience that the movement of qualified personnel between government and industry is far more often a benefit to the taxpayer than it is a detriment. Flexibility must also be provided for the appointment of noncareer executives to carry out the administration's programs. It should also be noted that, by law, the Under Secretary of Defense for Acquisition must be drawn from industry. Dual compensation laws limit the ability of the Department to hire experienced, knowledgeable military personnel into civilian positions when they retire.

VOLUNTARY DISCLOSURE OF FRAUD

Senator NUNN. In 1986, DOD began a much-publicized program to encourage contractors to voluntarily disclose fraud and other wrongdoing. Should the "voluntary disclosure" program and self-policing policies be made mandatory?

Secretary CARLUCCI. The voluntary disclosure program and self-policing policies should not be made mandatory. DOD encourages Defense contractors to adopt a policy of voluntarily disclosing potential civil or criminal fraud matters affecting their contractual relationship with the DOD as a central part of their corporate self-governance program. This policy was instituted in 1986 by DOD as a part of the implementation of the recommendations made by the Packard Commission in that section of its report to the President concerning "Industry Accountability: Contractor Self/Governance." This policy encourages companies to establish procedures urging employees to report to the company or the DOD IG any suspected instances of fraud and report other matters to the Defense Contract Audit Agency or the appropriate contracting officer.

The disclosures are made with no advance agreement regarding possible DOD resolution of the matter and with no promises regarding potential civil or criminal actions by the Department of Justice (DOJ). Prompt voluntary disclosure, full cooperation, complete access to necessary records, restitution and adequate corrective actions are key indicators of contractor integrity.

Of the largest defense contractors, 46 companies have established a self-governance program as part of the Defense Industry Initiative (DII). I have written a letter to the top two hundred defense contractors requesting that they establish a self-governance program, if they have not done so already and to report to me concerning their program. I am convinced that the best way to ensure ethical behavior by our contractors is to encourage voluntary programs, not by establishing mandatory ones.

CONFLICTS OF INTEREST

Senator NUNN. What guidance have you issued to prevent the conflict of interest that can arise when a consultant to a contractor also serves on a military advisory board? What type of information relating to conflicts of interest, if any, are consultants to defense contractors required to provide to DoD?

Secretary CARLUCCI. All individuals appointed to Department of Defense Advisory Committees, whether serving with or without compensation, are required to file DD Form 1555, "Confidential Statement of Affiliations and Financial Interests." This is helpful to the advisory committee staffs to insure that persons are not appointed if they have conflicting interests and, for those who are appointed, to alert them and the members of the committee staff to areas of potential problems as they may arise during the deliberations of the committee.

All advisory committee members are briefed on the Standards of Conduct and are reminded that they risk the consequences of prosecution under criminal law (18 U.S.C. §208) if they participate as special Government employees on matters in which they or their employers have personal financial interests.

Senator NUNN. Section 2397c of Title 10 of the U.S. Code requires all contractors with contracts greater than $10 million to submit an annual report to the Secretary of Defense listing all former DoD employees and officers compensated by the contractor and to identify various aspects of their employment, including a complete description of their work on each major defense system. The Secretary of Defense is required to assess the accuracy and completeness of the reports that have been filed. How many violations have been identified? How many persons have been considered for the administrative penalty of up to $10,000, imposed by the Sec Def, which attaches to a knowing failure to file such a report?

Secretary CARLUCCI. Although this law was passed in October of 1986, its effective date was April 16, 1987 and the first contractor reports were not required until April 1 of this year. We are in the process of compiling those reports and digesting their contents to identify potential violations of the filing requirements as well as violations of other standards of conduct laws. We are not ready at this point to name any violators.

Senator NUNN. DOD Directive 5500.7 requires special Government employees to file Form 1555, Statement of Affiliations and Financial Interests. Are all individuals employed by a consulting firm who work on a contract with the Department of Defense considered special Government employees for purposes of this Directive and thus required to submit Form 1555? If not, are such individuals otherwise required to submit to DOD the information required by Form 1555 with respect to clients and financial interests? Describe the process and criteria for determining the disclosures that a consulting firm must make as to conflicts of interest. Is a consulting firm required to list all of its clients and financial interests?

Secretary CARLUCCI. Only the individuals appointed consultants are considered "special Government employees" and thus are required to file the financial disclosure forms (DD Form 1555). Employees of consulting firms who are not individually appointed are not required to disclose their financial interests. Consulting firms are not required to identify all of their clients.

This particular financial form (DD Form 1555) was designed for full-time Department of Defense officers and employees. Most of the forms are filed by persons in the GS/GM grade ranges of 13 through 15. The DD Form 1555 has been reviewed in light of the current controversy and it is recognized that it has shortcomings when used to collect information from consultants. It will be re-designed to make it more clear to consultants that they must identify their clients.

Implicit in this question is the assumption that a more comprehensive disclosure system would better protect the interest of the Government and the taxpayers. We doubt that premise. It is unlikely that there can be designed a disclosure system that will compel dishonest persons to confess past or planned misconduct.

DOD USE OF CONSULTANTS

Senator NUNN. What guidance have you issued to ensure that the current accounting system for collecting data on consultants and their costs is adequate?

Secretary CARLUCCI. The DOD Directive on Contracted Advisory and Assistance Service (CAAS) requires each DOD Component to record all CAAS obligations into their accounting system in accordance with the DOD Accounting Manual. These accounting systems provide an audit trail for tracking information on individual

CAAS contracts. The DoD Inspector General in accordance with the United States Code. Title 31, Section 1114(b) conducts an annual evaluation of DoD actions in instituting effective management controls for CAAS and in improving the accuracy and completeness of this accounting system. An audit entitled "The Status of Consulting Services" (Report Number 88-184) dated July 22, 1988 has just recently been completed.

SOURCE SELECTION AUTHORITY

Senator NUNN. DOD Directive 4105.62 designates the Service Secretary as the Source Selection Authority (SSA) and makes the SSA responsible for ensuring that conflicts of interest are avoided and premature or unauthorized disclosure of source selection information is avoided. What procedures are used by the SSA to perform these functions?

Secretary CARLUCCI. The Source Selection Authority approves the source selection plan which is prepared by the Program Manager. The SSA also appoints the Source Selection Advisory Council (SSAC). As indicated above, persons involved in the source selection process are subject to specific rules and guidelines. They are informed of this guidance before the source selection process begins. They are also required to agree in writing to the rules on non-disclosure of source selection sensitive information.

DISCLOSURE OF SOURCE SELECTION INFORMATION

Senator NUNN. DOD Directive 4105.62 does not prohibit the disclosure of the membership of the source selection team prior to contract award, but suggests that such disclosure is imprudent. Should such disclosure be prohibited?

Secretary CARLUCCI. An outright prohibition against disclosure of the membership of the source selection team may not be practicable. Certain members of the team, such as the contracting officer, will be known because they must interface with the contractors and with other government personnel in the performance of their duties. Other members will be detailed for the duration of the source selection. Potentially, controls could be established similar to those used with highly classified activities. To be effective, these controls would add to the cost of the activity. Furthermore, they cannot guarantee that there will never be a willful circumvention of the rules.

Senator NUNN What would be the advantages and disadvantages of eliminating the incentive for consultants to try to get insider information by removing the insider information in the first place and making it available to all contractors up front?

Senator CARLUCCI. It may appear advantageous to remove the existence of "insider information" to preclude the misuse of that information. However, to disclose proprietary information to all competitors would destroy the essence of competition which is to select the one proposal, on the basis of price and other factors such as technical and operational performance, that can best meet the Government's needs.

REMOVING THE INCENTIVE TO CHEAT

Senator NUNN. As part of the source selection process, the Military Department first determines what criteria it will establish to evaluate contractors proposals, and then separately establishes a set of numerical values or "weights" which are assigned to the various criteria. The Services apparently tell the contractors what the criteria are, but we do not tell them what weights have been assigned to the criteria. What is the rationale for not telling the contractors what the weights are at the same time they are informed of the criteria?

Secretary CARLUCCI. The exact weights are not disclosed to offerors or to evaluators to preclude the temptation for either party to introduce an intentional bias into either the proposal or the evaluation. All parties are apprised of the relative ranking of weighted factors.

BEST AND FINAL OFFERS

Senator NUNN. One of the issues that has arisen is whether consultants were able to get one company's original bid and give it to their competitors so that they could tailor a better "best and final offer"?

Secretary CARLUCCI. As indicated above, the rules that are in place regarding source selections are intended to preserve the integrity of the process. Disclosure of the strengths and weaknesses in all proposals would lead to technical leveling, technical transfusion, and consequently to auctioning because source selection then becomes dependent solely on cost or price proposals. This would weaken effective design competition at the front end of the acquisition process where present practices reward innovation and ingenuity. It these incentives were removed, we could expect technical proposals to gravitate toward a "lowest common denominator." Why work hard if one's work product is confiscated?

Senator **Nunn**. In your testimony, you suggest that increased competition in the acquisition process may have caused "difficult problems that are just now surfacing." Do you believe that there is now too much competition in defense contracting?

Secretary **Carlucci**. We do not have too much competition, but I am disturbed by the inordinate amount of attention that is directed to source selection. We must have a fair and effective system to select the best source for the job in our judgment. However, through Congressional direction, political lobbying and intense marketing, the source selection process can be redirected away from obtaining the best value for meeting mission requirements into a winning-is-everything mentality. To meet this challenge, we have been focusing on what is actually produced after source selection. We must continue to emphasize contract performance since this determines the quality, price and capabilities of the systems.

Dr. Costello has instituted several initiatives to focus on getting the best value for the taxpayer while putting the right equipment into the hands of the troops. His total quality management approach keeps the contractors focused on improvements in how well a system performs. Could cost is a technique for stripping away non-value-added procedures to give us what we need, not what some bureaucracy thinks *it* needs. Streamlining peels away the many layers of specifications to allow the contractor and the program manager to concentrate on what is essential to the success of the mission. I intend to continue to look at ways we can redirect the marketing energy poured out through the legislative process as well as within the executive branch by contractors to ensure that the best way to win new work is to have a top-flight record of past performance on previous comparable systems. Only by making people demonstrate their capabilities in this way can we ever hope to really improve the acquisition process. A government contract should not be anyone's right, but something earned through quality performance.

PRE-AWARD CERTIFICATION

Senator **Nunn**. In your testimony, you indicate that your task force will suggest the "establishment of a pre-award certification to be required of contractors whose conduct, as established through official information, warrants enhanced review." What type and sufficiency of evidence will be needed to require such a certification?

Secretary **Carlucci**. We have adopted a pre-award certification for use by contractors named in the ongoing investigation to assure they have not improperly or illegally obtained source selection information pertaining to a contract to be awarded. This action is required before any contract over $100,000 is awarded to them. The purpose of this certificate is to assure we do not award any new contracts that are "tainted" while not denying contracts to offerors who are innocent of wrongdoing.

Questions Submitted by Senator Edward M. Kennedy

COST OVERRUNS

Senator **Kennedy**. A recent GAO study reported that 19 of 22 shipbuilding programs had exceeded the contract target price. What is the status of those programs now?

Secretary **Carlucci**. In testimony before the Subcommittee on Defense Committee on Appropriations, House of Representatives, on April 19, 1988, the GAO updated its report GAO/NSIAD-88-15 of October 16, 1987. The GAO testified that, as of February 1988, the Navy's estimate as to how much above target the contracts in question would be completed had increased by 18% since the GAO report was published.

FUTURE EMPLOYMENT OF CONSULTANTS

Senator **Kennedy**. What regulations govern the future employment of these consultants and support contractor personnel? Specifically, do the regulations restricting passage through the revolving door between DOD and the defense industry apply to them?

Secretary **Carlucci**. Legislation enacted in 1962 recognized that persons serving in the Government on a part-time or intermittent basis should not be subject to all of the rules applicable to regular employees. This explanation was given in the report of the Senate Judiciary Committee in reporting on the bill that became Pub. L. No. 87-849:

> Most of the existing conflict-of-interest statutes were enacted in the 19th century—that is, at a time when persons outside the Government rarely served it in this way. The laws were therefore directed at activities of regular Government employees, and their present impact on the occasionally needed experts—those whose main work is performed outside the Government—is unduly severe. This harsh impact constitutes an appreciable deterrent to the Government's obtaining needed part-time services.

Consultants are the outside experts who serve the Department of Defense under these rules. When they are appointed to temporary or intermittent positions in the Department they become "special Government employees" under the Standards of Conduct laws and the implementing regulations of the Department of Defense. The principal law is 18 U.S.C. § 207, implemented by DOD Directive 5500.7, "Standards of Conduct," and regulations of the various DOD components. Depending upon the duties they perform within the Department, these special Government employees may be subject to limitations on where they work after their DOD service ends and on any representational responsibilities they perform for future employers. They also may be required to report their future employment relationships.

DEFENSE CONTRACTOR

Senator KENNEDY. Are these consultants that DOD employs to assist with bid preparation and evaluation required to disclose which defense contractors that they are also advising?

Secretary CARLUCCI. The preparation of bids, of course, is a contractor function and not a Department of Defense function. The evaluation of bids and proposals, on the other hand, is done by DOD officers and employees, sometimes with the assistance of consultants.

As noted earlier, if consultants are appointed to positions in the Department of Defense they become "special Government employees" under the Standards of Conduct laws and the implementing regulations of the Department of Defense. These persons are required to file Defense Department form 1555, "Confidential Statement of Affiliations and Financial Interests." In that form they will identify their employers. If they are consultants for more than one employer, all should be identified.

DOD USE OF CONSULTANTS

Senator KENNEDY. Is it true that the Pentagon position of Director for Contracted Advisory and Assistance Services has been vacant for 16 months?

Secretary CARLUCCI. The position of DOD Director of Contracted Advisory and Assistance Services (CAAS) has never been left vacant. Although a permanent replacement has not been appointed since the previous director left in April 1987, there has been an Acting Director of Contracted Advisory and Assistance Services in charge of the office which has been performing the oversight functions. The paperwork to permanently fill this position is being processed and the position should be filled within the next several months.

PROCUREMENT PROCESS TAMPERING

Senator KENNEDY. Have you begun to assess how we might ensure that no contractor profits from any tampering with the procurement process?

Secretary CARLUCCI. We have adopted a clause for use in contracts with those sources named in the investigation allowing the government to recover profit should it subsequently be determined the contractor obtained that contract improperly or illegally. We have provisions in all our contracts that allow termination for default and entitle the Government to damages if it is determined that a contractor offered or gave a gratuity to a government official. If termination for default is determined not to be in the government's best interest, a reduction in contract price can be negotiated in lieu of termination. We can suspend or debar contractors from receiving federal contracts if they do not have a satisfactory record of integrity.

RECOUP PROFIT FROM ILLEGAL ACTIVITY

Senator KENNEDY. Specifically, would it be possible as a threshold remedy for the Government to recoup any profit from a contract that was obtained through illegal activity?

Secretary CARLUCCI. Yes. A clause entitled "Profit Recapture for Illegal or Improper Activity" is included in all contracts that exceed $100,000 issued with those contractors named in the ongoing investigation. The clause allows the government to reduce the contract price by the amount of any anticipated profit or ten percent of the contract price, whichever is greater, if (i) a person or business entity is convicted of bribery; graft; conflicts of interest; conspiracy; theft of public money, property, or records; false statements; fraud; or fraud by wire; (ii) the Secretary or designee determines that any officer, employee, or agent of the contractor obtained from the government any source selection information concerning the contract prior to award; or (iii) the prices in the contract were not arrived at independently; the prices in the contract were knowingly disclosed by the contractor to any other offeror or competitor before award; or the contractor attempted to induce any other concern to submit or fail to submit an offer for the purpose of restricting competition.

QUESTIONS SUBMITTED BY SENATOR STROM THURMOND

BALANCE BETWEEN INDUSTRY AND GOVERNMENT

Senator THURMOND. Mr. Secretary, there needs to be a proper balance between industry and the government. Industry needs to be regulated, but too much bureaucratic regulation can unnecessarily increase costs. How would you assess the balance in today's environment?

Secretary CARLUCCI. In the last six years, Congress has enacted at least 15 laws that have substantially reformed the procurement system. The magnitude of this legislation and the changes that have been required have resulted in hundreds of new rules and regulations that workers in both the government and industry must try to follow. Enactment of a new law or issuance of a new rule for each and every problem that may be found to exist in the system is not needed or desirable as each new law and rule tends to complicate the procurement system further, limits our flexibility to take actions to meet ever changing situations and restricts the judgment making ability of our acquisition personnel. This has been the real impact of the legislation enacted over the last six years on the procurement process. We need to work together to simplify the process by eliminating the legislative and regulatory burdens that have been allowed to accumulate. We need to return responsibility, accountability and the incentive for initiative and innovation to our procurement professionals and those in industry.

DEFENSE ACQUISITION PROCESS

Senator THURMOND. Mr. Secretary, have various Congressionally mandated reforms of the procurement process and those called for by the Packard Commission been implemented, and if so, have they been successful?

Secretary CARLUCCI. Congressionally mandated procurement process reforms such as the Defense Acquisition Reform Act of 1986, and those called for by the Packard Commission have been implemented or are in the process of being implemented. Multiyear procurement is a good example of one that we have been working hard on for several years. Increasing multiyear procurement was one of the Carlucci Initiatives in 1981, has been called for by Congress, and was one of the Packard Commission recommendations. Total savings from multiyear procurements since FY 1982 will exceed $7.5 billion. In the FY89 DoD budget, DoD proposed six multiyear candidates with total savings of $869 million.

Several of the Packard recommendations require continuing management attention, such as program stability, increasing DoD's use of prototypes in the acquisition process, and increasing effective competition. We now have the Under Secretary of Defense for Acquisition, and the Vice Chairman of the Joint Chiefs of Staff working closely together at major acquisition program decision points to ensure implementation of these reforms.

Long-term activities such as enhancing quality of acquisition personnel and eliminating any nonessential management layers also require continuous scrutiny and probably can never be considered completely finished.

ABSENCE OF REGULATION AND OVERSIGHT

Senator THURMOND. Mr. Secretary, in your opinion, is the current problem related to as absence of regulation and oversight, or human greed?

Secretary **Carlucci**. I believe the current problem is caused by human greed. We have an abundance of regulations and oversight requirements in place. However, I have directed the DoD Task Force to identify any changes to our acquisition system that should be made as a result of what we learn from the investigation. My instructions do not limit the nature of the change. Nothing is sacred—neither organizational structure, regulations, nor the need to change existing law.

DOD USE OF CONSULTANTS

Senator **Thurmond**. Mr. Secretary, it has come to our attention that the Department of the Navy utilizes consultants to a far greater degree than the other services. Could you shed some light on this for the committee?

Secretary **Carlucci**. The total dollars reported spent on contract support services in fiscal year 1987 for the Army, Navy and Air Force are $.4, $2.0, and $1.0 billion respectively. A direct comparison of these numbers cannot be made since each service maintains their own accounting system; and despite the fact that the same defintions are being used, there is room for the services to interpret what is and is not included in the report. We have initiated an effort to standardize the reporting of CAAS in order to overcome these differences.

COMPETITION

Senator **Thurmond**. Mr. Secretary, the defense industry in this country can basically only sell to the Government. We do not sell defense materiel to the public, so the idea of competition is competition in a very constrained environment. To what degree, in your opinion, does this lead to the sort of problem we are experiencing now?

Secretary **Carlucci**. Tagging competition as the root cause of what is wrong with the system just is flat wrong. I would agree that competition does not make sense in all cases, such as where the cost of maintaining two or more sources exceeds any expected program savings, and we have continually taken that view in our policy and regulatory statements. However, Congress made it clear some years ago through the Competition in Contracting Act (CICA) that all responsible sources are to have the opportunity to bid on government requirements. Another aspect of CICA is that bidders were given certain rights to stop any procurement with a protest to the General Accounting Office (or the General Services Board of Contract Appeals for ADP). This gives our bidders rights far beyond those available in any government system we know, let alone the commercial world. Because of the ability of any disgruntled bidder to stop a procurement dead in its tracks, perhaps the system has overcompensated by requiring much more documentation than before. This doesn't mean competition is wrong, just that each case has to be viewed on its own merits.

Mr. Packard recommended in his report a few years ago that we do more to encourage "commercial-style" competition. This was not clearly defined at the time, but we think it means encouraging long term competitive contractual relationships with proven suppliers. This is how most companies buy, and it makes sense. Unfortunately, the law does not permit us to use the commercial marketplace as a substitute for our highly regulated system. We have been working with the Office of Federal Procurement Policy to develop a commercial products law to send to Congress and it is just about ready to go. However, this doesn't help us with state of the art weapon systems for which there is no commercial equivalent. For these, we have been working to streamline the regulations, specifications and speed up the process. We have just issued new procedures which control the use of subsequent best and final offers and we continue to search for improvements that make sense.

Questions Submitted by Senator John McCain

CONGRESSIONAL MICROMANAGEMENT

Senator **McCain**. Could you provide summary statistics on the trends in Congressional micromanagement affecting procurement actions?

Could you provide a detailed list of congressional actions in the bills and reports affecting fiscal year 1989 procurements, and a summary of the problems that each of these actions has created for the Department and of its impact on the incremental cost and effectiveness of those procurements?

Could you provide similar data on the impact of the House and Senate authorization and appropriation bills and reports for fiscal year 1989?

Mr. CARLUCCI. Within the timeframe permitted we are able only to provide the following list of legislation having impact on DOD acquisition/procurement. We are reviewing laws enacted over the last six years and a response will be provided by separate letter to the Armed Services Committees.

PUBLIC LAW AND YEAR OF ENACTMENT AND TITLE OF LAW AND BRIEF DESCRIPTION

Public Law 98-72 (1983).—*A Bill to Improve Small Business Access to Federal Procurement Information.*—Amended the Small Business Act to revise synopsizing requirements.

Public Law 98-94 (1983).—*DOD Authorization Act for 1984.*—Among other things: Called for the use of Independent Cost Estimates for Major Defense Programs, established a Director for Operational Test and Evaluation and required a report to Congress on Spare Parts Management.

Public Law 98-212 (1983).—*Department of Defense Appropriations Act for Fiscal Year 1984.*—Among other things added procurement policy coverage for the first time that: Required DOD to obtain Weapons Systems Guarantees (warranties) from contractors and prohibited the purchase of commercial products if a small business would be rejected due to lack of commercial acceptance of its item.

Public Law 98-369 (1984).—*Competition in Contracting Act.*—Among other things: Revised terminology for contracting, set strict standards for obtaining competition, established revised protest procedures and revised synopsizing requirements.

Public Law 98-473 (1984).—*Department of Defense Appropriations Act for Fiscal Year 1985.*—Among other things added procurement policy coverage for the first time that: Prohibited initiation of full scale engineering development of a major system prior to notification to Congress of a competitive procurement plan or the reasons why not and required notification of Congress of Multiyear contracts with an economic order quantity in excess of $20 million.

Public Law 98-525 (1984).—*Defense Procurement Reform Act of 1984 (part of the DoD Authorization Act of 1985).*—Among other things: Established requirements for the use of prequalification procedures, provided controls and requirements governing technical data, set rank and grade for competition advocates, established tours of duty for Program managers, established rules for allocating overhead to spare parts, established rules governing the commercial pricing of spare parts (lowest commercial price), revised and codified requirement for weapons systems guarantees passed under Public Law 98-212 required identification of suppliers and sources of items provided under contracts and called for various reports to Congress.

Public Law 98-577 (1984).—*Small Business and Federal Procurement Competition Enhancement Act.*—Among other things: Required mandatory publication of procurement regulations in the Federal Register for a public comment period, revised synopsizing requirements, and provided for the placement of Small Business Administration Spare Parts Breakout representatives in major DoD acquisition centers.

Public Law 99-145 (1985).—*Defense Procurement Improvement Act of 1985 (part of the DoD Authorization Act for 1986.*—Among other things: Codified the description of allowable costs under DoD contracts, required dual sourcing of major defense programs, codified requirements for Should Cost analyses, set "Revolving Door Rules," set penalties for overcharging by contractors and directed the use of "Work Measurement Standards" in certain contracts.

Public Law 99-190 (1986).—*The Omnibus Appropriations Continuing Resolution for 1986.*—Required employment of Alaska and Hawaiian residents in military constructions contracts in those states, and revised allowable costs description enacted under Public Law 99-145.

Public Law 99-433 (1986).—*Department of Defense Reorganization Act.*—Among other things: Required procurement policy staffs of Military Department to be organized at Secretarial level.

Public Law 99-500 (1986).—*The Omnibus Appropriations Continuing Resolution for 1987 and Defense Procurement Improvement Act of 1986.*—Among other things added procurement policy coverage for the first time that: Established the duties of the Under Secretary of Defense for Acquisition restricted undefinitized contractual actions, revised law pertaining to to commercial pricing for spare parts (P.L. 98-525), revised the Truth in Negotiations Act, provided preference for nondevelopmental items, revised progress payment rates, established competition requirements for the acquisition of prototypes of major systems, revised technical data requirements and expanded ADP protest procedures within the General Services Administration for DOD contracts.

Public Law 99-661 (1986).—*DoD Authorization Act of 1987.*—Among other things: Duplicated the Defense Procurement Improvement Act of 1986 and established a 5 percent of procurement, R&D and construction dollars authorized goal for the award of contracts to minorities and authorized the payment of a 10 percent premium for the purposes of achieving this goal.

Public Law 99-634 (1986).—*Anti-Kickback Enforcement Act of 1986.*—Prohibits subcontractor kick-backs to government prime contractors.

Public Law 100-180 (1987).—*National Defense Authorization Act for Fiscal Years 1988 and 1989—Title VIII, Acquisition Policy.*—Among other things: Provided for Congressional Oversight of cost of schedule variances in certain programs and authorized Congress to consider programs as milestone authorization despite not having been identified as such by the SecDef, amended the Truth in Negotiations Act to revised definitions previously revised under P.L. 99-500, directed that contracting officers' performance evaluations include their ability to increase awards to minority firms, substantially revised the law pertain to rights in technical data, established rules governing contractor costs for special tooling and special test equipment and placed restrictions on the purchase of foreign made administrative motor vehicles.

Public Law 100-202 (1987).—*The Omnibus Appropriations Continuing Resolution for 1988.*—Among other things added procurement policy coverage for the first time that: Restricting purchases from Toshiba and Kongsberg Vsapenfabrikk, required a ten day advance notification to Congress prior to terminating multi-year contracts, required the USD(A) to approve all fixed price R&D contracts with a value of $10 million or more and limited the acquisition to domestic sources of: certain class of machine tools, mooring and anchor chain, super computers and equipment items that use textiles.

BILL NUMBER AND TITLE OF BILL AND BRIEF DESCRIPTION

H.R. 4264 Conference Report.—*National Defense Authorization Act, Fiscal Year 1989—Conference Report* Includes the following:

Integrated Finance Policy—§ 801.

Requires establishment of a long term plan to ensure that DOD profit policies are kept current.

Requires a yearly report to Congress on efforts to prevent excess profits.

Establishes a Public/Government Advisory Committee to consider the profit issue and report to Congress on their findings.

Evaluation of Contracts for Professional Services [*Uncompensated Overtime*]—*§ 804.*

Requires the SecDef to establish criteria for use in the award of contracts that do not encourage the use of uncompensated overtime.

Establishes an Industry/Government Advisory Committee to consider how to do this and report to Congress on their findings.

Department of Defense Advisory Panel on Government Industry Relations—§ 808.

Establishes an Industry/Government Advisory Committee to consider ways to enhance DOD and industry cooperation on such matters as self-governing oversight programs, debarment procedure, and alternative disputes procedures.

Requires the Panel to report to Congress on their findings.

Regulatory Simplification and Streamlining of Oversight Activities—§ 809. Requires a report to Congress on internal DOD efforts to streamline acquisition procedures.

Incentives for Innovation—§ 806.—Rights in Technical Data—prohibits the DOD from requiring prime contractors to submit proposals that will enable the U.S. to acquire competitive items that were developed at private expense.

Guidance on the Use of Fixed-Price Development Contracts—§ 807.—Revises and codifies requirement for approval of fixed price contracts by the USD(A) previously enacted as part of the FY 88 Appropriations Act.

Standards for Contractor Inventory Accounting Systems [MRP]—§ 834.—Requires the Department of Defense to establish a policy governing inventory accounting systems that are already in existence and requires contractors certification of the system.

EXAMPLES OF REPETITIVE LEGISLATIVE CHANGES AND LEGISLATION THAT CODIFIED EXISTING REGULATIONS/POLICIES

Examples of repetitive legislative action in specific topical areas are:

Synopsizing of Procurement Actions

Public Law 98-72(1983).—A Bill to Improve Small Business Access to Federal Procurement Information.

Public Law 98-369(1984).—Competition in Contracting Act.

Public Law 98-577(1984).—Small Business and Federal Procurement Competition Enhancement Act.

Rights in Technical Data

Public Law 98-525(1984).—Defense Procurement Reform Act of 1984 (part of the DOD Authorization Act for 1985).

Public Law 99-500(1986).—Defense Procurement Improvement Act of 1986.

Public Law 100-180(1987).—National Defense Authorization Act for Fiscal Years 1988 and 1989—Title VIII, Acquisition Policy.

H.R. 4264(1988).—National Defense Authorization Act, Fiscal Year 1989—Conference Report. Section 806 prohibits the DOD from requiring prime contractors to submit proposals that will enable the U.S. to acquire competitively priced items that were developed at private expense.

SPECIAL ACQUISITION SERVICE

Senator McCain. What are your views regarding the creation of some special defense acquisition service or special branch of the civil service?

Secretary Carlucci. I strongly oppose the creation of a special acquisition service. However, the Department of Defense has been a leader in advocating improvements in our civilian personnel systems.

The administration has proposed to Congress adoption of the Civil Service Reform Act to make changes throughout the Government based on experience gained through the Navy's China Lake model.

This model involves pay banding and streamlining personnel administration to allow more focus on managing the individual instead of paper job descriptions of what our employees do and has become associated with several efforts known as the alternative personnel system.

The alternative personnel system offered by Senator Bingaman in March as S. 2254 would have permanently authorized DOD to implement the China Lake model for up to 300,000 DOD civilians.

We supported this concept.

Since there was not full support for S. 2254, Senator Bingaman agreed to modify his proposal to allow a continuance of a test of personnel improvements for 100,000 DOD personnel in 4 separate test projects with another 6 test projects spread throughout the Government.

This is not as attractive as the earlier bill, since it doesn't build on our earlier successes and will not cover the entire acquisition workforce.

We see the need for bold action on the part of Congress to provide the tools for improving the workforce.

The initial Bingaman proposal brought us closer to that. However, since the test substitute bill is a step in the right direction and appears to be the most that can be attained at this time, we support it and the administration supports it.

Chairman Nunn. The hearing is now adjourned.

[Whereupon at 12:15 p.m., the hearing was adjourned.]

DEFENSE ACQUISITION PROCESS

WEDNESDAY, JULY 27, 1988

U.S. Senate,
Committee on Armed Services,
Washington, DC.

The committee met, pursuant to notice, at 9:40 a.m., in room 216, Hart Senate Office Building, Senator Sam Nunn (chairman) presiding.

Present: Senators Nunn, Exon, Bingaman, Dixon, Glenn, Gore, Shelby, Warner, Thurmond, Quayle, and McCain.

Staff present: Arnold L. Punaro, staff director; Romie L. Brownlee, deputy staff director; Patrick A. Tucker, minority counsel; Andrew S. Effron, counsel; Gerald K. Bankus, Jonathan L. Etherton, Sherri Wasserman Goodman, John J. Hamre, George K. Johnson, Jr., Ronald P. Kelly, James P. Locher III, Daniel J. Wildfong, professional staff members; Barbara L. Braucht, Pamela G. Powell, Mickie Jan Wise, staff assistants.

Also present: Jeffrey B. Subko, assistant to Senator Exon; Peter K. Levine, assistant to Senator Levin; William J. Lynn, assistant to Senator Kennedy; Edward M. McGaffigan, Jr., assistant to Senator Bingaman; Charles C. Smith, assistant to Senator Dixon; Milton D. Beach and Donald A. Mitchell, assistants to Senator Glenn; Leon Fuerth, assistant to Senator Gore; Terrence Lynch, assistant to Senator Shelby; Dale F. Gerry, assistant to Senator Cohen; Henry D. Sokolski, assistant to Senator Quayle; Mark J. Albrecht, assistant to Senator Wilson; and Anthony H. Cordesman, assistant to Senator McCain.

OPENING STATEMENT BY SENATOR SAM NUNN, CHAIRMAN

Chairman Nunn. The committee will come to order.

This morning the committee continues its hearings on the defense acquisition system. In our first hearing the Comptroller General of the United States, Charles Bowsher, made it clear the defense acquisition system is plagued by serious management deficiencies.

At our second hearing Secretary of Defense Carlucci noted—and I quote—"The ongoing military procurement investigation understandably raises questions about the health of our defense acquisition system." And he acknowledged that—and I quote—"There are deficiencies in how America equips its forces."

The Secretary's judgment reflects the view expressed 2 years ago by the President's Blue Ribbon Commission on Defense Management, and I quote from the Packard Commission. "The defense acquisition system has basic problems that must be corrected. These problems are deeply entrenched and have developed over several decades from an increasingly bureaucratic and overregulated process. As a result, all too many of our weapon systems cost too much, take too long to develop, and by the time they are fielded, incorporate obsolete technology."

Today we are fortunate to have with us the Chairman of the President's Commission, Dave Packard, and a member of the commission, Mr. Jim Woolsey, to help us put the current acquisition issues into perspective. Mr. Packard's previous service as Deputy Secretary of Defense, his outstanding leadership in industry and his many contributions to public service are well known and appreciated by members of this committee. Mr. Woolsey, a distinguished attorney in private practice, has served as Under Secretary of the Navy and also as General Counsel to this committee.

The Packard Commission noted that—again I quote—"Chances for meaningful improvement will come not from more regulation, but only with major institutional change."

This committee has taken a leading role in implementing those aspects of the Packard Commission's recommendations directed at Congress. In 1986, for example, we initiated legislation establishing the position of Under Secretary of Defense for Acquisition. In 1987, we adopted a 2-year defense budget. Although this effort fell short of legislating a complete 2-year program, it provided a major start which greatly simplified this year's legislative process.

We have reduced congressional micromanagement as evidenced by the fact that our committee's report, which was 490 pages long in 1986, was only 181 pages long in 1988. As we recognize in our report, the acquisition system is suffering from regulatory overload as a result of numerous legislative and internal changes in recent years. We have attempted to limit statutory changes to those modifications which can be made without creating an undue burden for either government or industry.

While there is much that we can do in Congress to improve our approach to defense acquisition issues, the ultimate responsibility for implementing the institutional changes recommended by the Packard Commission rests with the executive branch.

Interestingly enough, I left a meeting this morning talking about the desirability of the 2-year budget process, and talking about the redundancy of committee activities here on the Hill and how we can reduce that redundancy. We recognize full well that the way Congress handles the defense budget is far from optimum and that we need to do a lot of work ourselves while we're also looking very carefully at the way the executive branch handles their end of the picture.

Mr. Packard and Mr. Woolsey, we are delighted to have you here this morning. Before we get your opening statements, we will turn to Senator Warner for any opening statements he may have.

Senator WARNER. Mr. Chairman, I simply welcome my old boss, having served with him for many years in the Department of Defense, and also having worked on many projects with Mr. Woolsey.

I often think that if there's a Oracle of Delphi with respect to procurement, it is Mr. Packard. So, we're happy to hear from you today, Mr. Packard.

Chairman NUNN. Senator Dixon has a prepared statement that will be inserted in the record.

[The prepared statement of Senator Alan Dixon follows:]

PREPARED STATEMENT BY SENATOR ALAN J. DIXON

Mr. Chairman, today we are having our third hearing on the Defense Department's acquisition process. Our witnesses today are David Packard, Chairman of the President's Blue Ribbon Commission on Defense Management and former Deputy Secretary of Defense, and Mr. James Woolsey, a member of the President's Blue Ribbon Commission on Defense Management and a former Under Secretary of the Navy.

The June 30, 1986 report of the President's Blue Ribbon Commission recommended the creation of an Under Secretary with the powers to ". . . supervise the performance of the entire acquisition system . . .". I do not think that the present position of Under Secretary of Defense for Acquisition actually possesses the authority to "supervise" the entire Department of Defense Procurement System. As the Senator that introduced the legislation that created the Office of the Under Secretary of Defense for Acquisition, I have come to the conclusion that this position needs to be raised to that of a Deputy Secretary of Defense for Acquisition. I feel that if we are to have a true acquisition and procurement czar within the Department of Defense then he must only have to report to two individuals: the Secretary of Defense and the President. He should not have to report to a Deputy Secretary of Defense.

In his statement today, Mr. Packard points out that the Chairman of the Joint Chiefs of Staff ". . . has the authority to override the other Joint Chiefs in deciding what military weapons and systems to procure." This same authority should be given to the civilian acquisition czar. Mr. Packard then says in his speech ". . . that the Commission intended to give—the top individuals in acquisition—the message that there should be only one chain of command in acquisition, and apparently they did not get the message . . .". The legislation I have introduced does just that. It places these senior acquisition officials under the acquisition czar and requires their confirmation by the Senate. In the future, these men and women will be strictly responsible for acquisition matters within the services and the service secretaries will not be able to appoint themselves to this position.

Mr. Packard, just one last observation. You point out in the closing of your speech that price alone should not be the only factor in purchasing a product. I agree with you and so do my colleagues. We realized that the services were considering price above all else when awarding a contract so we simply placed the word "quality" in the beginning of the requirements in the competition section of the law. Now I think it is up to the Department of Defense to make sure that this is followed.

Thank you Mr. Chairman.

Chairman NUNN. Mr. Packard, why don't you go ahead.

STATEMENT OF HON. DAVID PACKARD, FORMER DEPUTY SECRETARY OF DEFENSE, CHAIRMAN OF THE PRESIDENT'S BLUE RIBBON COMMISSION ON DEFENSE MANAGEMENT

Mr. PACKARD. Mr. Chairman and distinguished members of the committee, I appreciate very much your invitation to be here again. Frankly, I thought I could get out of this problem and let some of the younger ones do all the work, but these recent issues and your invitations encouraged me to get back in and help a bit.

I want to say I'm very pleased to have Jim Woolsey here with me. He is not only a very important member of our commission, but I've worked with Jim before on some of these issues and I have a very high respect for his knowledge and judgment.

I want to thank the committee again because you people on this committee were very helpful in the work of our commission. You've done a great many things in the interim that have been moving toward the implementation of the things we were recommending.

I'm going to be perhaps a little bit critical. I'm going to do so and turn some attention to these matters, but I don't want to imply that this is any criticism of any individuals involved.

I'm not going to read my statement here. I'm just going to touch on a few highlights, and I think if you have time you can read it.

I want to begin by saying the things I'm going to talk about today deal largely with the major acquisition problems. There are lots of difficulties in low level procurement actions, shoddy goods, cheating, fraud and theft and all those kinds of things. I don't see any course in dealing with those other than what's being done here. You have to get inspectors and auditors and people of all kinds and root out these problems and try to deal with them in ways that will not only bring appropriate justice, but will also provide some measure of deterrence for those continued activities.

I want to say in particular that I very strongly endorse Secretary Carlucci's testimony before this committee on July 12. He said very much the same things to the House committee yesterday. I think that the five guideposts he has are about right. I wouldn't agree with everything that he said just as I'm sure that everything that I did when I was there wasn't right. So, this is a difficult issue, but I think he is going precisely in the right direction.

He has pointed out the many intervention points that are available to influence decisions. That is what invites these kind of problems that cause our recent attention here. To the extent those can be limited, it would be very, very desirable.

Now, there are two or three things we must keep in front of us. The most important of all is that there has been a very large improvement in the morale and quality and therefore, the strength of our military forces during these past 7 years. And while this is a result of a rather substantial increase in the budget, particularly from 1981 to 1986, this improvement in our military strength has enabled the United States to deal from a position of strength as a leader of the Free world. We should all be very thankful that this was done.

I think progress in negotiating with the Soviets—actually the indications that we may have some influence in the Persian Gulf even with respect to Iran—indicates that our military strength has been a very important factor.

Above all, we should not use this effort to improve our acquisition process to reduce our military strength. We need more military capability than we now have to deal with all the affairs in this troubled world. I hope that everyone involved in military reform will keep that in mind.

This recent military buildup has been accompanied by more disclosures of waste and inefficiency, and I think until recently the efforts to deal with those things have been somewhat counterproductive. But I think the work of this committee and the things we're going to talk about today indicate that there has been some progress.

There is one other issue I wanted to raise before you here and that is that this increase in defense expenditures has been a contributor to our Federal budget deficit. Now, you can argue that entitlements and other things were more important, but it seems to me that we need to look at every aspect of our Federal budget because I strongly believe that the health of our economy is a very important factor, together with our military strength, in determining the ability of the United States to be the leader of the Free world.

Now, the underlying cause of these acquisition problems—you can try and oversimplify it, but they're not simple—is that procurement has been micromanaged to death, and in my opinion the attempts to deal with these problems have almost criminalized the activities in this area.

The country has long-established legal procedures to deal with crime. They should not be preempted in the name of military reform. In my opinion, to do so results, or tends to result at least, in actions of a kind that might be expected only in a tyrannical type of a police state. And such actions are the antithesis of the very fundamental concepts of a free society and a free enterprise economy. It is very hard for me to understand frankly how this came about during an administration that is dedicated to free enterprise.

Now, I think it's very important not to overreact on these recent allegations, and I will talk about that in some detail further on.

I have a case here in respect to the Varian Associates which, if you want to talk in some detail, we can do so, but I won't say anything further about that.

I do want to bring to your attention some observations that have been made by a law firm that has been involved in this military acquisition business for a long time. Those quotations are on page 5 of my statement, if you'd like to follow this. It's the firm of McKenna, Conner & Cuneo. And I quote here two statements they made. The last paragraph of the first one is the only one I want to read here to emphasize.

They say, "In fact, there have been more changes in laws and regulations affecting the industry in the last 7 years than there had been in the previous 25 years." And as far as I can see, they have not been effective. In many ways the situation is worse as a result of all these actions rather than better.

Now the second statement I want to read in its entirety. It reads as follows. "Congress has not come to grips with the nature and the dimensions of their responsibility. First it loudly proclaims that industry should be guided by the principles of free enterprise, capitalism and competition which have shaped all industry in our country. Then it sets out to legislate and regulate the industry to such a profound extent as to make the application of these principles utterly impossible." I would certainly strongly endorse that statement.

Unless these procedures can be changed to put the incentives back in the right place, the situation will only continue to deteriorate. And I say this despite the fact that I know there are encouraging numbers of areas of improvement.

Now, I've outlined what some of the previous reports have said. I won't talk about those in any detail, but I do want to talk about this matter of the need for more attention to our worldwide military strategy.

That, as I think this committee will remember, was an important issue that was addressed by the commission. We said at the time that "Today there is no rational system whereby the executive branch and the Congress reach coherent and enduring agreement on national military strategy, the forces to carry it out, and the funding that should be provided—in light of the overall economy and the competing claims on national resources." We added something to that, but I just wanted to point out several facets that relate to that recommendation.

First, in many ways the most important is the lack of adequate consideration by both the executive branch and the Congress as to what our worldwide military strategy should be.

Second, is the pressures of the military services to promote their individual strategies and their pet weapons.

Third, is the practice of the Congress to appropriate funds for military equipment and programs on a year-by-year basis. That's an issue I know this committee has been addressing, and it's a very important issue.

And fourth, is the practice of the Congress to appropriate funds for military equipment and military bases that are not needed by military forces. Now, I know that's a touchy subject for a good many people, but I want to state it in very straightforward terms.

I think that, as I say here on page 8, there is another devastating effect of this disgraceful congressional practice of funding programs for equipment that is not really needed by the military forces. It uses taxpayers' money specifically for the personal benefit of the Members of the Congress. And it is, therefore, fundamentally unethical behavior. How can the Congress expect ethical behavior from the DOD and the defense industry when it sets a bad example of ethical behavior at the top?

Now, I'm very pleased to see the progress this committee has made. I know that you're moving ahead on the important job of trying to attract, retain and motivate better qualified people in this whole acquisition process. And that raises another issue which I did not touch on here.

I'm very pleased to see that Senator Bingaman made some very constructive comments about this subject in the discussions on the committee's report this year, and that is that the Federal laboratories, like China Lake, Naval Research Laboratory, and the others, are very important. They have made some very useful contributions to the strength and capability of our military forces in the past. There has been a tendency for these laboratories to be downgraded. There is a great deal of pressure from the industry to get these laboratories out of business because they, in effect, compete with some of the research and development in industry. And, in fact, they have often demonstrated that some of the research industry proposals are faulty in one way or another.

So, I would encourage you, in addition to looking at the importance of keeping good scientists and engineers on the staff of these laboratories, to also continue to give some attention to keep these laboratories in the picture because they can make a very important contribution to improvements along the line.

Now, the same law firm that I mentioned before made some comments about the involvement of the military people in acquisition. I think it is very desirable, perhaps even essential as I say in my comments, to keep the involvement of military people in acquisition. But I think if they are involved, they must be officers who have opted for a career in procurement. This commission has observed that it has become quite clear that the DOD acquisition process has become too complex to be managed by military non-careerists who will be rotated to other unrelated assignments as often as every 2 years. No amount of intensive training will equip such individuals, no matter how bright and well-intentioned, to cope with this process.

In my opinion, the same principle applies to lawyers at the secretarial level. As a matter of fact, that was one of the reasons that the commission made the recommendation to establish an Under Secretary position to be filled by a person with appropriate education and experience to oversee the entire military acquisition process. That office has been established, thanks to the support of this committee, and it is occupied now by someone who I consider to be a capable person.

I recently attended an all-day meeting at Fort Belvoir, which was sponsored by Secretary Carlucci and planned by Bob Costello. It was the first time that all of the top acquisition people in all of the services had met together to discuss these acquisition issues. I was most pleased by the enthusiasm and the level of good common sense at this meeting although I did not agree with everything that they said.

I made a comment to them that I think in some way they did not understand the recommendations of our commission. They are still talking, as I indicated on page 9 and 10, about the question of several chains of command in each one of the service organizations. I told them that our commission's recommendation was that there should be only one chain of command, and I didn't think they got the message.

Now, on page 10 I mentioned another comment about the number of people in the DOD acquisition process. I said that the only way to deal with this issue may be for the Congress to mandate a reduction in the order of 20 percent in the number of people in DOD and in the services who are involved in acquisition. I want to emphasize that I said "may be." I think without any question a better job could be done with 20 percent fewer people.

This raises some issues, of course, because you could get the wrong people out of the process in doing this and you could make it worse if it were not done wisely and carefully.

When such a reduction is being considered, it would be a very good idea for Congress to think about the same thing with respect to their congressional staffs. I'm sure we won't get a lot of enthusiasm about that subject from perhaps even members of this committee.

I do think this is an issue that must be addressed somewhere along the line. If it can be addressed carefully, I think it could result in some very significant improvements in the process.

Now, I mentioned comments about some previous experience on this, the McNamara times and the total package procurement. I think some of you know we were involved in the results of those policies when I was at the Department from late 1969 to 1970. And I think that this misplaced emphasis on competition, which has been the recent practice here, is very likely to end up with the same result.

The emphasis on competition on the big programs has been far too much involved in paperwork, tons of paperwork, describing how the bidder would meet a bunch of Mickey Mouse requirements. And as I've said—as many times that I've looked at this subject. I think if you had a list, and you put the names of the qualified bidders on the wall and threw darts, you'd probably come out with just as good an answer and it would save a lot of time and a lot of money. Now, I know that's not practical. But that just indicates that we've got a lot of complexity in this process that is counterproductive.

I've called your attention to the two programs that in my opinion were the best managed programs that I have known anything about or learned anything about in this whole business, and those were the Minuteman program and the Polaris program. They were done in the late 1950s before the Secretary of Defense was involved in procurement.

That, of course, suggests two options. One is to get the Secretary of Defense out of the procurement business, and I don't think that is realistic. But if you get them down to the place where they are determining policy and are able to enforce policy and they're not trying to do all the work themselves, it would be constructive.

Now, the other lesson from those two early examples of good acquisition practice is that they were done with small teams of highly competent people. These people were put in charge. They were given the responsibility and the authority to do the job, and they were left alone. That's why those programs were successful. Every time you look at this issue, you come back to the conclusion if you could just get a team of knowledgeable people assigned to these programs, so that they work with the programs long enough to really have a big impact, this would probably do as much as anything else to improve our acquisition program.

I don't think we need some major changes. I've commented about the completely civilian procurement organization here. That's an issue we talked about in the commission. I don't think it's possible to implement such a system in this country. Besides, the British system doesn't work very well either.

I noticed in the Wall Street Journal yesterday a comment about the defense acquisition system in France, and that I think perhaps may be an example of something that's important. They have a professional military corps involved in procurement there. These are people who devote their careers to procurement and their careers are determined by their performance in the procurement area not by how well they do things in other important military assignments.

That, in a sense, is very much in the direction of what we were trying to achieve in recommending this reorganization and working with you on this reorganization of the Chairman of the Joint Chiefs—getting the Vice Chairman there, getting the Under Secretary for Acquisition there—to get a group of professional people at the top who could look at these issues and do so in an objective way and override some of the service influences and the other influences. I think that can be very important.

Another suggestion that has been made is to nationalize some of the companies that are involved in the acquisition business. I don't think that really makes very much sense either. It would be very hard to nationalize enough of the industry to make much of a difference.

The only concern I have is it seems to me that there is a very high probability, if these recent practices of continuing to require contractors to make heavy investments in facilities and equipment, to cost-share research and development, to break down procurement into uneconomical packages and so forth—it has been estimated that the unfunded liabilities of the industry are already over $10 billion as a result of these practices. I see no possibility whatsoever of the industry generating the level of funding to meet those requirements unless these practices can be changed.

Chairman NUNN. Mr. Packard, I read that in your statement last night. I read your whole statement.

Could you give us an example of what you mean by defense industry unfunded liability so we'll make sure we understand what you're talking about in terms of the $10 billion?

Mr. PACKARD. Well, the simple thing is the investment in facilities that would be required. Investment in facilities can be made by any sensible business management on the basis that those facilities will in the future produce enough profits to be able to finance the investment and hopefully improve the profitability of the organization. That is the best simple example of the case.

There's nothing wrong in asking contractors to make better investments in facilities for the development and production of military equipment, but to do it under a system in which they have no possibility of recouping their investments is counterproductive. It won't work. That's what I mean.

I think it's very desirable for us to go back and look at some of the things that have been done in the past. Secretary Carlucci made a very important point: let's try and build on some of the experience we've had in this business, and not all the experience is right. But I think we ought to go back and look more carefully at some of these past practices.

Cost plus contracts with incentives based on performance have been used for complex new development programs. It is simply not possible to know what the cost is going to be for a complex new weapon system that has never been developed before. To expect anybody to make a front-end commitment on that is basically wrong.

I think you ought to go back and look at this prototyping issue again. That was one of my pet projects when I was there. If you go back and look at the F-16 and the F-17 programs, those turned out very well. The A-10 program, the radar on the AWACS was done under a prototype competition. They got a better radar for that program as a result of that. That approach requires more up-front funding, and for that reason, the services and the Congress have been unwilling to give that very much support. But I really think you ought to look at that issue again.

I think there is a great opportunity for more use of commercial products. That was a point we made in our commission's recommendations. There are some cases where commercial products are not only cheaper but more reliable than military products. We ought to take advantage of those.

There has been a very bad aspect of this issue and that is the practice of requiring companies which have developed a product with their own funds to make the technical information available to the Government so the Government can set up someone in competition with them to show that there is some competition in the matter. I think that's a very unsound principle. Certainly anyone in his right senses would not undertake to enter into such a contract with the Government.

There are intermediate issues, and like everything else, there are no completely simplified problems with these programs, but that's something that should be done.

There's another issue that is very important. There are some places where there should be sole source contracts. One example is for contracts for university research. Such contracts should be undertaken when there's a specific scientist or a group of scientists in the university that has something to contribute to the subject. To put such contracts as that out for competition is absolutely stupid and we shouldn't do it.

I know, you've talked about this last and best offer issue, and I'm pleased to see Secretary Carlucci moving on that. I've alluded to that as being essentially running the military acquisition like an Iranian bazaar, and that's not the way we really ought to be running this business. So, I would encourage you to continue to work on that last and best offer thing. That just encourages people to try and go out and find out what the other guy's last issue has been.

While I'm on that subject, I want to add a matter that I think is relevant. I've been involved in this procurement business now for just about 48 years. I got started in 1940 and it was in a very low level.

But during that entire period, it has been well known that you could find out what the other guy's bid was. I was never quite smart enough to figure out how to do this on many occasions, and I found out it didn't make all that much a difference anyway. But I think all this issue about somebody being able to find out what the other guy did—we ought to be a little careful in looking on that as a major crisis. We ought to think very carefully about what's involved.

It seems to me the most important aspect in addressing this problem is we must deal with the fundamental causes of these difficulties, not with the symptoms. There has been a great tendency to deal with the symptoms and not really think about the basic causes. I think we have some very good progress in what is being done. And I again want to commend the committee, but we're not where we should be by any means.

In conclusion, I want to make some observations about competition in the private sector because I think these need to be kept in mind when you're talking about competition in military acquisition. Price is seldom, if ever, the only factor in purchasing a product or in awarding a contract. The quality of the product is almost always more important. The support and service the supplier can provide are also more important than price alone. The recent emphasis on competition in military acquisition has put price alone far too high on the list of determinants for awarding a contract. I hope this committee will endeavor to correct this bad situation.

Mr. Chairman, that concludes the summary I'm going to make of my remarks. Whether you want to proceed with questions or have Mr. Woolsey present his testimony, I would be glad to proceed.

[The prepared statement of Mr. Packard follows:]

TESTIMONY

BY

DAVID PACKARD, CHAIRMAN OF THE BOARD

OF

THE HEWLETT-PACKARD COMPANY

I appreciate the opportunity to appear before this distinguished committee to discuss the acquisition of military weapons, equipment and material. I am very pleased that Jim Woolsey is here with me. He was an outstanding contributor to the work of the Commission I chaired in 1986 and we have worked together on this subject before.

This Committee was very helpful during the work of our Commission and has been constructive in working to implement the Commission's recommendations. I want to thank you on behalf of all of the members of the Commission for the support you have given our recommendations.

While there has been some progress in putting our recommendation into effect, the recent disclosures about the extensive investigations of defense procurement, some of the problems the Navy is having in the Gulf and other problems that keep showing up emphasize the fact that our country still has a problem of major dimension in managing the defense establishment.

My remarks today will be largely my personal views. I have discussed what I plan to say only in a limited way with several other members of the Commission.

I am going to make some critical observations about this situation and I want you to know I will be talking about the major new weapons acquisition programs, and the military strategy that drives them. I know there are many abuses to be found in the vast number of low level procurement transactions, shoddy goods, cheating of nearly every kind, fraud and theft. I think what is being done is the only way to deal with those problems. Inspector generals, auditors, professional investigators must do everything possible to identify the real criminals and bring them to justice, and try to do so in ways that will help to deter such action in the future. The losses in this area are not large as a percentage of the amounts being spent or as a percentage of the number of transactions, and they can never be completely eliminated. They are not large either in comparison with the waste and inefficiences in the major acquisition programs.

In dealing with this subject it is important to understand that many of the things that come to light are not the problems but rather are symptoms of the problems. It will do no good to deal only with the symptons, the underlying causes must be identified and corrected.

I strongly endorse Secretary Carlucci's testimony before this committee on July 12. The five guideposts he recommended for reform are the right way to go. The intervention points where contractors can influence decisions on military acquisition invite abuse by the Contractors, by the Department and by the Congress. As many of these as possible should be eliminated.

There are some very important overall considerations that must be kept in front of everyone who is trying to deal with these defense acquisition problems.

First and most important of all --- there has been a very large improvement in the quality and the morale, and therefore the strength of our military forces during the past seven years. This has been the result of a substantial increase in the Defense Budget, a 100% increase in real dollars since I left the Pentagon in 1972. Most of the increase was between 1981 and 1986. This improvement in our military strength has enabled the United States to deal from a position of strength as the leader of the free world. We should all be thankful this was done. Above all we should not use the effort to improve our military acquisition to reduce our military strength. We need more military capability than we now have for the United States to provide leadership in this troubled world.

Second, this recent military build up has been accompanied by more disclosures of waste and inefficiency, and until recently attempts by the Congress and the Department to deal with waste and inefficiency have been counter productive.

This increase in defense expenditures has been a major contributor to the increase in the Federal Budget deficit which is at a level that weakens our otherwise strong economy.

It looks as though we will end up spending about two and a half trillion dollars on Defense between 1980 and 1990. That is two thousand five hundred--billions of dollars. If we had made only a five percent improvement in the way we spend our defense dollars our federal budget deficit could have been 125 billion dollars lower.

I strongly believe that the health of our economy is a very important determinate together with our military strength in the ability of the United States to lead the free world.

The underlying cause of these problems in military acquisition is that defense procurement has been micromanaged to death, and in effect criminalized during the past seven years by the combined actions of the Defense Department and the Congress. The actions that have been taken in defense procurement by the Adminstration and the Congress, assigning too many inspector generals and auditors to the major acquisition business, bringing criminal action against people like Jim Beggs, using information obtained by wire tapping offices in the Defense Department and the Defense industry for instant debarment and other punitive action against contractors, are going in the wrong direction.

This country has long established legal procedures to deal with crime. They should not be preempted in the name of military reform. To do so results in actions of a kind that would be expected only in the most tyrannical type of a police state. Such actions are the antithesis of the very fundamental concepts of a free society, and a free enterprise economy. It is very hard for me to understand how this came about during an administration dedicated to free enterprise.

I believe it is very important not to overreact to these recently disclosed allegations. Let me give you just one example of the dangers of instant reaction.

One division of the Varian Associates Company was accused of buying information from a consultant that enabled the division to under bid the competitors and win a contract. Almost as soon as this was disclosed someone in the Navy advised all procurement people in the Navy that the entire Company has been debarred and that no contract or business of any kind should be given to any division of the Company. While this was an internal memorandum it was leaked and Defense Contractors thought they, too, were to stop all business with Varian. When the top people in the Navy learned about this knee-jerk reaction, they realized that it was a serious injustice and I am sure it will be corrected as soon as possible.

It is difficult to see that any real damage was done in this case. The Defense Department got a better price on the contract and no one has charged that Varian was not well qualified to do the job. A representative was charged with stealing information from the Department and selling it for personal gain and some people in the Company were charged with buying the information. The charges should be dealt with by established legal procedures. The people who might be guilty should be tried and the punishment determined by the courts.

In my opinion, the Department, the Administration and the Congress together have created an environment in which honest and efficient military acquisition is impossible to implement.

The law firm of McKenna, Conner, & Cuneo has had more experience in DOD acquisition affairs than almost any other law firm in the country. It has been continuously involved since the early 1950's. I want to quote for you two passages from a recent report they have made on the subject.

"Over the past seven years, we have seen both a rapid growth in defense spending and an even more dramatic growth in the imposition of new laws and regulations on the Aerospace and Defense Industry. In fact, there have been more changes in laws and regulations affecting the industry in the last seven years than there had been in the preceding twenty five years."

"Congress has not come to grips with the nature and the dimension of their responsiblity. First it loudly proclaims that the industry should be guided by the principles of free enterprise, capitalism and competition which have shaped all industry in our country. Then it sets out to legislate and regulate the industry to such a profound extent as to make the application of these principles utterly impossible."

Unless the procedures can be changed to put the incentives back in the right place for the DOD and for the Defense Industry the situation will only continue to deteriorate. I say this despite the fact that I know there is an encouraging number of areas of improvement.

As you know there have been many studies of this problem over the past twenty five years and they nearly all have made similar recommendations. Professor J. Ronald Fox, a member of the Harvard Graduate School of Business has devoted his career to this subject. He notes that studies on this subject repeatedly urged Congress and the Defense Department to corrct five basic deficiencies:

1. Setting requirements for the most sophisticated systems attainable often irrespective of cost;

2. Underestimating schedules and costs of major programs, distorting the decision making process for the allocation of the national budget; (I would add deliberately doing so.)

3. Changes in programs and contract requirements caused by changes in military user preferences, leading to annual or more frequent changes in program funding levels, initiated by Congress and the DOD itself;

4. Lack of incentives for contractors and government personnel to reduce program costs; and

5. Failure to develop sufficient numbers of military and civilian personnel with training and experience in business management and in dealing with industrial firms to oversee the development and production of enormous, highly technical industrial programs.

Our commission made recommendations relating to all five of these issues. One of the most important recommendations of our commission was on National Security Planning and Budgeting which relates to establishing the requirements for major military equipment and systems, and minimizing the changes in programs and funding levels. The Commission defined the problem as follows:-

"Today there is no rational system whereby the Executive Branch and the Congress reach coherent and enduring agreement on national military strategy, the forces to carry it out, and the funding that should be provided - in light of the overall economy and competing claims on national resources. The absence of such a system contributes substantially to the instability and uncertainty that plague our defense program. These cause imbalances in our military forces and increase the costs of procuring military equipment."

There are several facets that relate to this recommendation. One is the lack of adequate consideration by both the Executive Branch and the Congress as to what our world-wide military strategy should be, a second is the pressures of the military services to promote their individual strategies and their pet weapons, and the third is the practice of the Congress to appropriate funds for military equipment and programs on a year by year basis, and the fourth is the practice of the Congress to appropriate funds for military equipment and military bases that are not needed by our military forces.

Some important steps have been taken to deal with these issues. This Committee deserves a great deal of credit for the progress that has been achieved. The role of the Chairman of the Joint Chiefs has been strengthened so that he now has adequate authority to exert a positive influence in developing a "coherent and enduring" national military strategy. He also has the authority to override the other Joint Chiefs in deciding what military weapons and systems to procure. While these are important steps nothing significant has come of them yet.

We do not yet have a coherent and enduring military strategy. The Commission on Integrated Long-Term Strategy has developed an excellent report on what a better military strategy might be. It is entitled "Discriminate Deterrence" and it seems to me to be a good start in developing a more coherent and enduring national military strategy, but I have not heard about any serious discussion of this proposal or any other proposal to do what the Commission recommended. I have not seen any evidence either that the Chairman in his new role has had much influence in getting the services to put their self interest aside to achieve an overall more effective military capability.

We expected it would take some time for the Chairman to do these important things in his new role. He must develop an adequate staff to support him. He must overcome bureaucratic tradition and service tradition, and to do this he must have strong continuing support from the President, the Secretary of Defense and the Congress. I know the Chairman has had many other important things to do during the past two years. I can not, however, give anyone very high marks for the implementation of this important recommendation of the Commission so far.

A two-year budget and multi-year funding of major programs are absolutely necessary to implement enduring agreement on military forces, and as I am sure you know billions of dollars would be saved. I know there has been some strong support for a two-year budget and multi-year funding by this committee, but the appropriation committees have so far refused to support a two-year budget or multi-year funding. The excuse I have heard is that there are so many problems in defense procurement that the Defense Department can not be trusted and must be monitored year by year. The real reason the Congress will not approve multi-year funding, in my opinion, is that to do so would severely limit their "pork barrel" opportunities. I can see only one way to deal with the selfish "pork barrel" practices of the Congress. They must be brought to the attention of the people all across the country. If the voters can be made aware of the magnitude and the seriousness of this problem, perhaps it can be brought under better control.

There is another devastating effect of the disgraceful Congressional practice of funding programs for equipment that is not really needed by our military forces. It is using taxpayers money specifically for the personal benefit of the members of the Congress and thus it is fundamentally unethical behavior. How can the Congress expect ethical behavior from the DOD and the Defense Industry when it sets such a bad example of ethical behavior at the top!

I do not believe we can ever get our money's worth from the billions of dollars we are spending on defense until we find some way to get better agreement on our world wide military strategy. There is no way to acquire an optimum set of military weapons, equipment, and facilities without better agreement on our strategy. If the Congress could bring itself to a two-year budget cycle, there would be more time for our strategy to be properly debated. Less costly, more effective military forces would certainly be the result.

The Commission pointed out the obvious fact that DOD must be able to attract, retain, and motivate well qualified acquisition personnel. This is a subject that has been discussed extensively. It involves, among other things, the role of Military people in the process, the "revolving door issue", and the all important question whether we really need to have as many people in DOD and the Services as are now involved in the military acquisition process.

I believe the involvement of military people in acquisition is essential but if they are involved they must be officers who have opted for a career in procurement. The McKenna, Conner, & Cuneo report puts it this way; "It has become quite clear that the DOD acquisition process is far too complex to be managed by military non-careerists who will be rotated to other unrelated assignments as often as every two years; no amount of intensive training will equip such individuals (no matter how bright and well intentioned) to cope with the process."

In my opinion the same principle applies to lawyers at the Secretarial level. That was essentially the reason the Commission recommended the establishment of an Under Secretary position to be filled by a person with appropriate education and experience to oversee the entire military acquisition process. That office has been established and it is occupied by a capable person. I recently attended an all day meeting at Ft. Belvior, which was sponsored by Secretary Carlucci and planned by Bob Costello. It was the first time the top acquisition people from all of the services had been together to discuss acquisition issues. I was most pleased by the enthusiasm and the level of good common sense at this meeting, although I did not agree with everything that was said.

They had at this meeting a paper entitled "Assessment of the similarities/differences between the service acquisition organization". This paper indicated that they still plan to have three or four chains of command involved in each of the service acquisition organizatiions, which is manifestly absurd. I told them that the Commission intended to give them the message that there should be only one chain of command in acquisition, and apparenly they did not get the message. We realized that our recommendations would require some major changes from past practice, and that it would be difficult for people in the services to face up to a major change from what they have been doing in the past. I think so far they have flunked out on this issue.

It may be that the only way to deal with this issue is for the Congress to mandate a reduction in the order of 20% in the number of people in DOD and in the Services who are involved in acquisition. I am absolutely sure a better job would be done with 20% fewer people. I would not recommend such a reduction unless a corresponding reduction were made in the number of people on congressional staffs.

I do not like to be so negative about the progress that has been made in implementing the Commissions recommendations because I know there have been many positive steps in the right direction but they do not get at the heart of the problem. The breakdown of the procurement system is caused by two things, the attempt by the Congress to impose competition in a situation in which real competition in the conventional context is virtually impossible to achieve, and to try to impose competetion by a myriad of unrealistic rules and regulations enforced by what I consider to be identical to "police state" tactics.

The question about how to manage the development and production of major military weapons and systems has been a major priority of every Secretary of Defense since 1960. The McNamara solution was "total package procurement". This appeared to be an obvious solution, get a bid for the whole job at the beginning and then hold the contractor responsible. The problem was, and is, that it is impossible for anyone to know how much it is going to cost to develop and produce a complex new weapon system that has never been built before. Contractors would bid or negotiate the best deal they could to get the job. I spent considerable time when I was at the Pentagon trying to resolve the problems that resulted from this approach. I visited several Contractors who were in trouble, behind schedule and above cost on their programs. In several cases the work was in areas where I had some experience and after inspecting the work I usually met with the CEO of the company. In most cases, I told him I was sure he must have known at the time he made the bid that the price was too low and the delivery time was too short. When I asked him why he did this the reply was almost always "That was the only way we could get the job."

The misplaced emphasis on competition which has been the recent practice has had the same result. I know you can cite substantial savings from this so called competition and some of it has been real. On the big programs the competition however has been mostly in paper work, literally tons of paper work, describing how the bidder would meet a bunch of "mickey mouse" requirements that have absolutely nothing to do with doing the job right. One could do just as good a job, as I have said many times, in awarding the major contracts by putting the names of qualified bidders on the wall and throwing darts. This would also save a lot of time and money.

It is ironical but I think very significant to note that the two best management programs for the design and development of a complex new weapons system were the Minuteman Program and the Polaris Program. They were done in the late 1950's before the OSD was involved in procurement. That suggests two options, one is to get the CSE out of procurement management, the other is to put small teams of highly qualified people in charge of each major program, give them the responsiblity and the authority to do the job and then leave them alone while they are doing it. That was why those programs were so successful.

I do not believe it is necessary to make major changes in the system but I think it is useful to at least look at some of the other options.

One option is a completely civilian procurement organization to handle the procurement of all military weapons and systems for the services. This would be along the lines of the acquisition system used in Great Britian. Our commission considered this option and concluded it was not viable. There would be severe political opposition, it would be hard to attract, keep, and motivate enough good people to do the job well, given the existing civil service system. In addition the British system does not work very well.

It has been suggested that the defense industry should be nationalized, major production facilities converted into arsenals, owned by the government, but possibly operated by private companies in the same way some of our national laboratories are managed. This option would certainly have severe political opposition and there is no way in the world to nationalize enough of the defense industry to make any real difference anyway. It would also be in the face of world wide trends in the opposite direction. I believe, however, there is a high probability this will be the only option available for some of the major firms, if the present practice continues of requiring contractors to make heavier investment in facilities, cost share research and development, and in the name of competition require programs to be broken down to uneconomical packages so there can be two producers instead of one. It has been estimated that the unfunded liabilities of the defense industry resulting from these practices is already over ten billion dollars and under present contracting practices the industry has no possibility whatever of generating funds of this magnitude to cover these liabilities. A much simpler option would be to go

A much simpler option would be to go back to the contracting policies that have been used in the past. These would include cost plus contracts with incentives based on performance. The use of prototyping to provide legitimate competition on smaller systems and sub- systems is the best approach of all. It requires more funding up front but I would encourage this committee do what is necessary to suppport the use of prototyping whenever it can be used. More extensive use of commercial products will provide better equipment at a lower cost for many military products. The Defense Department is, however, way off base in requiring companies which supply commercial products to provide data rights so someone can be set up to compete with them for the products they have developed. There is a place for the placement of sole source contracts without competition. Contracts for research at Universities is a good example. In such contracts the Department needs the special expertise that is most often available only at a given University and to require competition is absolutely stupid.

Another practice that has been encouraged in the name competition is that of requiring repeated bids down to the "last and best offer". That practice should be stopped. It is operating military acquisition like an Iranian Bazaar. There are many good acquisition practices that we know will work well. The simplest and best thing the Congress could do to make a watershed improvement in military acquisition would be to add a large measure of common sense to the process. I want to compliment this committee for having done so, but so far the Congress as a whole is a long way behind.

It seems to me one approach that should be encouraged would be to find a more objective way to measure the performance of the defense contractors and to award contracts based largely on demonstrated past performance, rather than on paperwork proposals. To do this it would be necessary to establish the rules to evaluate past performance. I was very pleased to find this proposal being discussed at the Ft. Belvior meeting. The Air Force has already developed a good procedure to evaluate past performance and the other services have agreed to use the system.

If such a system were established and the contractors knew about the rules and penalties when the contracts were awarded it would be a real incentive for better performanes. Inspectors and auditors would still be needed but fewer would be required. I am quite certain that a system along these lines would get the entire acquisition business on a better track, and would provide our military forces with better equipment deployed more rapidly and at a lower cost.

I am convinced that a procurement program along these lines can be developed and that it will put the incentives for good performance in the right place. Fewer people would be needed in the DOD to manage such a program. It would be necessary for the Congress to refrain from influencing or overriding the selection of the contractor by the DOD. It would not subtract from the need for better strategic planning, in fact, it would give the DOD and the Congress more time to devote to strategic planning and it would still require program stability. Most important it would reduce much of the red tape and free the energy, enthusiasm and creativity of the talented people in the Defense Department and the Defense Industry to design and develop the best military equipment for our armed forces. I hope this committee will give serious consideration to an approach to defense acquisition along these lines.

In conclusion I want to make some observations about competition in the private sector. Price is seldom, if ever, the only factor in purchasing a product or awarding a contract. The quality of the product is almost always more important, and the support and service the supplier can provide are also more important than price alone. The recent emphasis on competition in military acquisition has put price alone far too high and I hope this committee will endeavor to correct this bad situation. That concludes my formal remarks and I will be pleased to try to respond to your questions.

Chairman **Nunn**. Thank you very much, Mr. Packard. I think we'll proceed to get to Mr. Woolsey's testimony and then come back and ask both of you some questions.

Mr. **Packard**. All right.

STATEMENT OF HON. R. JAMES WOOLSEY, FORMER UNDER SECRETARY OF THE NAVY, MEMBER OF THE PRESIDENT'S BLUE RIBBON COMMISSION ON DEFENSE MANAGEMENT

Mr. **Woolsey**. Thank you, Mr. Chairman. I also will not read my statement, which has been distributed. But I will, if it's all right, make a few informal comments highlighting some aspects of it.

I want to call the committee's attention to a quotation at the bottom of the first page of my statement from Bill Perry in the Armed Forces Journal last month, which I think is an excellent characterization of the current DOD acquisition system. He says: "It's too bureaucratic, too rigid, too adversarial, all wrapped up into one, making it one hell of an inefficient system, which is bad for the contractor but, even worse, I think it's bad for the Government."

Part of the problem has been the reforms themselves. And it's not reforms of a single type. Reform precisely targeted is a very valuable thing for the Congress and the executive branch to pursue. But as Florence Nightingale once said, in effect, "Whatever else hospitals do, they shouldn't cause disease." And so the first thing to make sure one is doing in reforming the acquisition system is not creating iatrogenic or physician-caused disease.

Part of the problem has been, at least in my judgment, that those with different positions, with different attitudes, toward what defense acquisition should be like—each acting in the country's best interest as he sees it—have often pushed a number of these reforms to such a great extent that you now have overlapping sets of requirements on both the Department of Defense and on defense contractors that are mutually exclusive.

To somewhat simplify this, I have suggested that there are two main schools of thought about how to fix defense acquisition. One is that defense ought to work somewhat like a highly regulated utility. And under that frame of mind, one looks at what we have today, for example: Some 20,000 auditors and inspectors in the Department of Defense. And in that frame of mind, one does what the Defense Department did a few years ago when the spare parts scandals hit. They added to that existing reinforced armored division worth of auditors and inspectors essentially another brigade, several thousand.

From another point of view, one can have in mind that defense acquisition should follow a model of perfect competition—a model that many of us studied at the beginning of econ 101 in college—that the market should be a completely free one, that it is probably one of largely fungible products, somewhat like commodities. It's a market in which there are virtually no barriers to entry.

Now, under this set of assumptions, it is really wrong to differentiate between one supplier and another, or between one seemingly similar product and another. Under this model not only should anyone be able to sell crescent wrenches and folding chairs to the military, but pretty much anyone ought to be able to sell software and fighter aircraft. And from this perfect competition model comes such ideas as cost-only competition, multiple best and final offers in contract negotiation, fixed-price development contracts, and some of the things that Dave was talking about, such as government ownership of rights in data.

It is impermissible in this second view to rely, for example, on a contractor's record of quality. It is all right for the Government, if it can get away with it, not to fund R&D fully and to leave much of it up to the contractor to see if he can get well later on a production run.

Part of the problem is that some of these attitudes have been pushed so far that the defense industry today is moving into a situation where people are leaving the business and those who are staying in the business are buying in. They are doing so to such an extent that, under some of these fixed-price contracts, exactly the kinds of problems are developing, as Dave pointed out, that developed with total package procurement back in the 1960s when we went overboard in the fixed-price direction.

When I was General Counsel of this committee 17 years ago, we had to bail out Grumman on the F-14 contract because of its fixed-price nature, and we had to negotiate in the late 1970s a number of very controversial bail-outs of shipbuilders because of overuse of fixed-price contracts. Those types of problems have, again, been stored up over the course of the last 6 or 7 years, and they will be with us over the course of the next few years.

Some unfortunate official from the Department of Defense will be sitting before this committee, I would predict, within 5 years, testifying before you why a number of these fixed-price development contracts—or fixed-price options for procurement of systems that were in very early stages of development when the options were signed—have to be restructured under 85-804 or otherwise. You will not be happy, and he will not be happy to be here.

It doesn't mean that one can't use fixed-price contracts. There's a place for them. There is a place for their vigorous use. But it does mean, as I think Dave was stressing, that it is particularly important for the whole range of a company's capabilities, its history, its quality control, its record of service and the rest, to be considered and considered fully when contracts are awarded. One cannot hire a high-priced consultant to go out and obtain for a company a better historical record of quality control. One might be able to hire a high-priced consultant to obtain illegally some information, but he can't falsely build your company's record and history.

Now, part of the problem is that with these two different types of reforms—the reform from the school of those who believe everything should be very highly regulated such as in a utility and the reforms from the school of those who believe that defense competition is just like competition in fungible goods and commodities—we have had these overlapping sets of reforms going off and on over the years. And when they are put in legislation, the reforms don't go away. They stay. Sometimes when they are regulatory, they stay as well. And one ends up with a situation in which you have the worst of both worlds. The current acquisition system is bureaucratic, intrusive, and stifles innovation just as does the regulation of most public utilities, and it imposes the down-side risks of competition without permitting many of the up-side gains from competition, such as innovation and creativity.

I compared it in the statement to the first car that I ever owned, which was a small, sporty sedan that I bought on the promise that it would perform like a sports car and be practical like a sedan. It turned out instead that it had a sports car's repair bills and a sedan's acceleration. [Laughter.]

This committee has taken the lead, as Dave said, for the last several years in trying to make some very tailored and measured contributions to reforming the system, working with precision. And I endorse in the statement what you have been doing and with respect to stability in defense programs, with respect to getting away from fixed-price development contracts, with respect to moving away from micromanagement, and particularly with respect to trying to improve the quality of the civilian personnel in the Department of Defense.

But in the middle of your efforts and the efforts to implement, I think rather slowly, the commission's recommendations in the Department of Defense there has come upon us this recent procurement scandal. The real question facing you particularly now, I think, is how to deal with that and to convince yourselves and the public that you are doing something positive with respect to avoiding fraud and some of the types of behavior that have initially been disclosed in some of the court filings in these cases, while at the same time not undercutting the positive and measured steps toward reform that you have been working so hard on.

It is going to be difficult because many aspects of defense acquisition absolutely require close teamwork, cooperation, and free exchange of information between industry, those handling the technical aspects of acquisition, and military users. There is a point in the process where you want the participants to step back and have an arm's length relationship with one another—at which information should not cross the line and should not change hands. That's the point of source selection.

The key thing to review during your consideration of what is coming out in this current investigation is: if it is determined that corruption has occurred, just how it has occurred, and whether or not you might be able, as Secretary Carlucci has testified, for example, to reduce the points of intervention by doing away with such things as multiple best and final offers.

My own judgment and experience—in some 9 years of working on these issues with this committee and in the executive branch and in 11 years in private law practice in Washington looking at them from another perspective—has been that normally, when administered by the uniformed military (as it has normally in the past been delegated to them) the source selection process has been cumbersome, yes, and it has certainly at some times been a question of whether we're buying the right things. But in the hands of the uniformed military, at least in my judgment, it has normally been honest.

Now, one of the things to look at is to see whether one of the things that has gone wrong within the current procurement scandal is that too many source selection decisions were pulled away from the uniformed active duty military, with their traditions of professionalism and service and integrity, and taken over by senior civilians in the headquarters of military departments. If so, then I would suggest to you, and to those who have introduced a bill to further centralize and civilianize in an acquisition corps defense acquisition, that the obvious cure for that situation is certainly not necessarily to further centralize and civilianize the source selection process.

Chairman NUNN. Mr. Woolsey, we have a vote on. I think if you could stop right there, we will come back in about 10 minutes. I think it would be better to take a break. So, we'll take about a 10 minute break.

[Recess.]

Chairman NUNN. Mr. Woolsey, why don't you take up where you left off. We apologize for the interruption, but they are unavoidable around this place.

Mr. WOOLSEY. Thank you, Mr. Chairman. I well remember. I will finish up in just another couple of minutes.

I think it's important that we stressed in the Packard Commission report that although it's true that the military cannot run the acquisition system alone, that important civilian contributions are absolutely vital, we did find that there had been a substantial improvement in the quality and training and length of service of the uniformed military in acquisition management over the course of the last decade. Much of that, I might add, has to do with some reforms that Dave started when he was Deputy Secretary of Defense, such as the management school and the rest.

I think that it is important to try to do with the civilians something parallel to what has been done with the military over the course of the last 10 years, in improving the quality and background and training. And here I would particularly commend this committee as a whole, especially Senator Bingaman, and the work that all of you have done in trying to improve the quality of the civilians involved in the Department of Defense in acquisition.

I think that one point where I would have a different emphasis than Dave is, I would not suggest imposing now a flat percentage cut on acquisition personnel. I think that it is important that, as reforms take place, as you begin to move to a more streamlined management of programs along the lines of what we recommended in the commission report, the so-called enterprise programs, where able senior civilian managers are able to waive unnecessary mil specs and procedural steps—that process, as well as buying more commercially available components and all the rest, should make possible some personnel reductions. But I think it is particularly important that the personnel that are reduced need to be not those who are doing a good job in acquisition, but rather those who tend to have the rather unproductive duties of observing, reviewing, advocating, listening to briefings, and the like.

In an early draft of our commission's report 2 years ago, which Dave appropriately referred to as the continuing Presidential Commission on Metaphors, I drew an analogy between the plight of a program manager being overwhelmed by all these reviewers and advocates and inspectors and people who need to be briefed and the plight of the apprentice in the old legend of the Sorcerer's Apprentice. The sorcerer's apprentice was, in the legend, overwhelmed by berserk actions of brooms, buckets, and mops that had magically gotten out of control, and, in their efforts to assist him, destroyed the shop that he was trying to clean up.

I think there is no doubt that we need fewer people in acquisition, but it needs to be fewer reviewers, advocates, inspectors and people who liked to be briefed—fewer brooms, buckets, and mops.

I think that after a year or so of delay, following our commission's recommendations, in the Department of Defense—during which some organizational changes were made, many of them required by legislation originating in this committee—some helpful policy changes are now finally beginning to be made under Secretaries Carlucci and Costello. The Contractor Risk Assessment Guide is a good beginning toward trying to focus investigation and oversight resources where the problems are.

I don't think it is so much the case, in spite of my earlier crack about a reinforced division of auditors and inspectors, that we need less oversight. What we need is to have it focused where the problems are.

The analogy that is appropriate is the way the Securities and Exchange Commission ensures accurate financial reporting by publicly owned American companies. The SEC doesn't do so by having their own auditors and inspectors in each and every board room to look over the shoulder of those who are putting together proxy statements and annual reports. What they do is to hold accountable the outside directors, the auditors, the counsel. And when something goes wrong, as it does from time to time in financial reporting, civil remedies ensue, and also criminal prosecutions where appropriate.

The current scandal in the Defense Department may turn out to have some parallels with insider trading scandals on Wall Street. In my view the Defense Department, together with the Department of Justice and the Inspectors General system and Members of the Congress, should try to use this crisis as an opportunity to move toward a more sensible model of oversight for defense industry by the Department of Defense.

This means seeing that the guilty are prosecuted and also holding companies legally accountable for the accuracy of much information that cannot practically be scrutinized by government personnel. It may also require developing some more appropriate civil remedies for use in disciplining wrongdoers so that it is not necessary, where it is inappropriate, to resort to the more drastic ones of criminal law, debarment, and suspension.

Mr. Chairman, thank you for inviting me today, and that concludes my formal statement.

[The prepared statement of Mr. Woolsey follows:]

STATEMENT BY
R. JAMES WOOLSEY
SHEA & GARDNER
MEMBER, PACKARD COMMISSION

Mr. Chairman, Members of the Committee, I am honored to be invited to accompany Dave Packard here today. I served on the Packard Commission and, with Dave, on the Acquisition Task Force chaired by Bill Perry. I have a supplemental statement to add to Dave's overall statement for the Commission. I would like to try to illuminate some of the overall attitudes behind our 1986 recommendations as they might be relevant to the current investigation and reform proposals.

I do not need to set out in detail for this Committee what continues to be wrong with the Defense Department's system of acquisition. The MAC Group's Report in March, the study by the Center for Strategic and International Studies here in Washington released in April 1987, and our own Packard Commission's brief follow-up report to the President in 1987 all agree on the essential problem. Bill Perry, Commission member and former Under Secretary of Defense for Research and Engineering summarized it in a recent interview in the June Armed Forces Journal in blunt words similar to those that Dave Packard has used today: "too bureaucratic . . . too rigid . . . too adversial all wrapped into one -- making one hell of an inefficient system, which is bad for the contractor, but, even worse, I think it's bad for the government."

The key question is what to do about it and, even more importantly, how can we be assured that our reforms don't make the problem worse? I believe Florence Nightingale once said, in effect, "whatever else hospitals do, they shouldn't cause disease." The same criterion should apply to the Executive's and Congress's reforms of acquisition. Yet this area of defense acquisition is rife with such iatrogenic, physician-caused, diseases. Not because the physicians haven't been doing their best as they see it, but because this is a terribly difficult and complex set of problems. Most of the cures for one malady will cause adverse reactions to other functions of the patient unless great care is used.

Too often it has been assumed that one fix for what ails defense acquisition will cure virtually every important problem if it is just pushed far enough. In this spirit, there are two main schools of thought about how to fix defense acquisition. I might call them the highly-regulated utility school and the perfect competition school. Those who subscribe to the highly-regulated utility school lean toward detailed regulation of defense industry as the answer to most problems. It is one reason why, when the high cost of some spare parts received such publicity three or four years ago, the Defense Department looked at the some 20,000 auditors and inspectors then available to it -- approximately equal to the combat elements of an armored division -- and added several thousand more -- approximately a brigade's worth. Those who subscribe to the perfect competition school lean toward believing that defense acquisition is like a free market, but a market of a very special kind -- a market in fungible products rather like commodities, a market in which there are no, or virtually no, barriers to entry. According to this school, there should be great suspicion of any alleged differentiation between one supplier and another and between one seemingly-similar product and another. Not only can, and should, anyone be able to sell crescent wrenches and folding chairs to the military in this view (on the basis of open, free competition in price alone), but the same should be true of software and fighter aircraft. From this school comes the philosophical underpinnings for cost-only competition, multiple Best-and-final-offers in contract negotiations, fixed-price development contracts, government ownership of rights in data (even when the government didn't pay for the data's development), and so on.

The problem is not that either of these models is entirely wrong. There are fungible, commodity-like products sold to DoD, billions of dollars' worth annually, for which the perfect competition model may be close to appropriate. And similarly there are some ways that some parts of industry can appropriately be treated as a highly regulated utility. But the difficulty is that each of these schools of thought has tended to prevail at different times in over-extending its favorite reforms until we have arrived at the present situation.

The relationship between DoD and industry now has most of the negative features of both highly regulated utilities and perfectly competitive markets, with few of the advantages of either. The current acquisition system is bureaucratic, intrusive, and stifles innovation -- as does the regulation of most utilities -- and it imposes most of the down-side risks of competition. It produces almost none of the stability enjoyed by most regulated utilities and very little of the positive incentives to lower cost and increase creativity that are the hallmarks of competition. The defense acquisition system is somewhat like the first car I ever owned, a small sporty sedan that I bought on the promise that it would perform like a sports car and be practical like a sedan. Instead it had a sports' cars' repair bills and a sedan's acceleration.

This Committee has taken the lead in the last several years to try to make some very precise and measured contributions to reforming this system. At the same time our Commission was deliberating you were crafting the Goldwater-Nichols bill. You have also recently reduced detailed management by the Congress. You have cut by more than a factor of four the line items changed in the budget and cut the size of your report by more than half. You have required a single integrated financing plan from DoD, discouraged the use of fixed-price development contracts, and required a timetable for regulatory simplification. You have worked for stability in Defense programs by promoting two-year authorizations. And in my judgment it is of special importance that you have pressed consistently for an alternative personnel system for DoD acquisition personnel. These efforts are quite consistent with our Commission' recommendations two years ago.

In the midst of this positive effort, however, has come the disclosure of a major investigation of defense procurement fraud by the FBI and the Naval Investigative Service. It is early to try to make judgments about the causes of the wrongful and illegal acts that have been alleged in some filings that have been made public. But the Secretary of Defense has recently made some reform proposals, and it is already clear that there is some interest in parts of the Congress in drastic action -- and not only vigorous prosecution of those who may be found to have committed indictable offenses.

Let me conclude by offering my judgment about several of these reforms that are now being proposed.

One that I would not endorse is the creation of a new civilian acquisition corps to manage acquisition from the Office of the Secretary of Defense. I would recommend against it for the same reason we did so during the Packard Commission -- it would tend to undercut the ability of military users of weapons and weapons developers to work closely together, with flexibility, to trade off cost, schedule, and performance on programs. In many (but not all) aspects of defense acquisition what is needed is closer cooperation and an easier exchange of information between developers and military users, not less.

One of the many complex and difficult things about defense acquisition is that many aspects of it do require close teamwork, cooperation, and a free exchange of information, while at other times (*e.g.*, source selection) an arms-length relationship must obtain. This free exchange of information -- and the importance of such cooperation in ensuring that Defense not get locked in to expensive and detailed requirements and specifications -- was at the center of many of our Packard Commission recommendations. There are about two contracting actions every working second of every working day in DoD. The mind reels at the prospect of trying to manage the *operation* of all of this -- as distinct from the *policy*, which should be centrally managed -- from the Office of the Secretary of Defense. In any case, if what turns out to have gone wrong in the current scandal is that the source selection process -- the decision of *who* is to be awarded a contract -- has been corrupted, it is important to look at how it has been corrupted. You will probably not be able to make a judgment on this yet, but at this point it does not appear that the primary problem was that active duty military officers were not properly carrying out their duties in source selection. In the nearly nine years that I have served in the executive branch or on the staff of this Committee closely following these issues, and the some eleven years that I have observed them from private law practice, I have always thought that the vast preponderance of source selections -- normally delegated to the uniformed military by a Service Secretary -- was fairly conducted. Source selection, scoring, and the like is a somewhat cumbersome process, and certainly it is another question whether at any point Defense is buying the right or wrong weapon. But when administered by the uniformed military most source selection has, in my judgment, been highly honest. I have so far seen nothing in the current scandal to convince me otherwise. If what turns out to have gone wrong is that too many source selection decisions were pulled away from the uniformed active duty military -- with their traditions of professionalism, service, and integrity -- and taken over by senior civilians in the headquarters of military departments, the obvious cure is not to further centralize and civilianize source selection.

It may be that you will want to take a hard look at the use of consultants in source selection (although other uses of consultants seem to me to be essential to the operation of the system). I would hope particularly that you would continue to pursue efforts to improve the quality and experience of civilians in acquisition -- Presidential appointees as well as career civilians -- as we recommended in the Commission report. But I would not further centralize and civilianize operational decisionmaking in an effort to deal with DoD's two contract actions per working second.

Nor would I, and here I may differ from Dave, impose now a flat percentage cut on acquisition personnel. First of all, if such is undertaken suddenly the chaos may well produce a further reduction in the numbers of those remaining people who, against all odds, are still in the system trying to make it work. The numbers of "doers" may decrease and the numbers of "reviewers" may relatively, or absolutely, increase. What is needed is a steady transition to streamlined programs where unnecessary milspecs and procedural steps are set aside by knowledgeable managers, as we recommended. This process should reduce work for some parts of the bureaucracy and should make possible some personnel reductions. But it is extremely important that the civilian personnel reforms that you have worked to bring about be in place first, so that cuts are made in those personnel who have unproductive duties, not across the board.

In an early draft of our Commission's Report two years ago, which was appropriately referred to the continuing Presidential Commission on Metaphors, I drew an analogy between the plight of a program manager being overwhelmed by all of the various reviewers, advocates, inspectors, and people who needed to be briefed, and the plight of the Sorcerer's Apprentice. The latter was, in the legend, overwhelmed by the berserk actions of the brooms, buckets, and mops that had magically gotten out of control and, in their efforts to "assist" him, destroyed the shop he was trying the clean up. There is no doubt that we need fewer people in acquisition, but it needs to be fewer reviewers, advocates, inspectors, and people who like to be briefed. So this transition needs to be managed by incentives to make the system and the personnel slots evolve in a proper way.

Some efforts have finally begun. I think that -- after a year or so following our report in which organizational changes, but few helpful policy changes, were made by DoD -- it is now the case that Secretaries Carlucci and Costello are making some sound beginnings.

For example, the new Contractor Risk Assessment Guide (CRAG) from DoD is an effort to monitor contractor self-governance and to put DoD's oversight resources where the problems are rather than everywhere. By the same token I think that it is a positive step -- as Mr. Bowsher recently reported to Congress for the GAO -- that the Securities and Exchange Commission is moving to enhance its ability to monitor contractors' internal controls in such a way that its oversight of contract specific data, as well as financial data, may be enhanced. CRAG and the SEC generally both appear to proceed from a different philosophy than that which has pervaded DoD in the past with regard to oversight of contractor performance.

The issue is, do you concentrate oversight or try to do it everywhere? If DoD continues to multiply its own observers and reviewers across the board in response to the current scandal, we will see no end to the need for them. But if the Defense Department is permitted to let others do the monitoring for it, where they do it properly, and to focus on problem areas, it can multiply its effectiveness manyfold. I might add that when the recent insider trading scandals broke on Wall Street, the SEC and the Justice Department did not abandon the approach of holding a company's directors, outside auditors, and attorneys responsible for a company's financial reporting. They did not seek to flood the boardroom of every publicly-owned company with their own inspectors and auditors. They continued the policy of holding companies responsible for their own reporting, moved to enjoin some wrongdoers and to see that others were indicted.

The current scandal in DoD may turn out to have some parallels to the insider trading scandals on Wall Street. DoD should, in my view, use this as an opportunity to move toward an SEC model. This means seeing to it that the guilty are prosecuted, but it may also mean holding companies legally accountable for the accuracy of much information that is not scrutinized in detail by government personnel. It may require moving toward the development of civil remedies for use to discipline wrongdoers where appropriate, rather than relying solely on the more drastic ones of the criminal law, debarment, and suspension.

I hope these suggestions have been helpful, Mr. Chairman. Thank you for inviting me to testify.

Chairman NUNN. I thank both of you.

I'd like to start off the questioning, Mr. Packard, with a question to you about the prototype model that you have emphasized as being the desirable way for procurement. Could you walk us through that procedure, how it works, the advantages of it and particularly contrast that method of procurement with what we have now often described as the best and final offer type?

Mr. PACKARD. Well, as you know, the present system for approaching a new weapons development program is to spend a great deal of effort and write some very complicated specifications about all the details of this proposed device they are procuring. What you really are interested in is what the ultimate performance of that weapon is going to be. And it seemed to us at that time, and it still seems to me now, that you really ought to concentrate on what you want this weapon to do, not all the details of how you're going to build it and so forth.

So, our prototype approach was to give at least two contractors some general guidelines of the performance you expected from this weapon. That was what was done in the F-16 and the F-17 program, not a lot of detail, but enough information so that both the contractors knew what the role of this weapon was going to be, some of the problems of the environment it was going to operate in and so forth, and then give them enough money so that they could proceed with the development and the production of a model, and be completely free from all of the detailed requirements, mil specs and all these other things in doing this.

If they had any sense—and, of course, they did—they recognized that in the long run some of these applications of military specifications had to be applied.

Then you have a fly-off and actually find out which one of the airplanes performed better. That was done and it turned out that the F-16 performed somewhat better. I think it was an objective test. It turned out, as a matter of fact, they both were very good airplanes.

Then you make the decision that the winner of that competition would be awarded the production. Now, that's possible in programs probably up to the level of a fighter aircraft. When you get into a bomber or a nuclear submarine or something of that type, that procedure is not feasible.

But recognizing that a big part of the big programs is involved in the subcontract work, then you apply this principle by requiring some of the key elements in the subcontract aspect of the program to be built in prototypes and competed against each other on a real basis, and then the equipment that performs best is selected.

And that, as I implied, was what was done with the radar on the AWACS program. It was too big to compete the AWACS completely, but the radar was a very key element. That system was determined not so much by how well the airplane flew, but how well the radar worked. So you were able to have a competition on that and actually produce two sets of equipment, try them out in the field, find out for sure which one worked better, and then move ahead on that basis.

It seems to me that that program still makes a lot of sense, and I would encourage the Congress and the Department very strongly to go back and look at that issue again.

Chairman **Nunn**. Let me ask this question. Let's say company A wins the fly-off. Their plane is selected. What then is the competitive feature? Where do you go from that point on to have some competition on the production contract?

Mr. **Packard**. Well, at that point you have a very critical decision to make. Is it going to be the winner take all, or are you going to give some part of the business to the fellow that lost in order to keep competition into it? That is a difficult issue. I myself think you're going to be better off to make the winner take all; that will be a stronger incentive for him to do a good job.

Chairman **Nunn**. Then it becomes a negotiated contract at that point?

Mr. **Packard**. I simply think you negotiate a contract at that point and put some continued performance milestones in it and evaluate his performance. I don't think you can go back and rebid a lot of the details. I just don't think it's feasible. You have a dilemma here because it may mean that the contractor who loses the bid is going to be in real trouble because he won't have any business to support what he may have put into the program himself. But I don't think you can have good competition without some real risk for the guy that is competing.

Chairman NUNN. Mr. Woolsey.

Mr. WOOLSEY. Mr. Chairman, let me just add one point. One of the reasons we recommended in the Commission that the Defense Advanced Research Projects Agency, DARPA, assume a rather larger role than it has in the past and get into prototyping was the extreme importance that we all attached to what Dave has said. I would simply stress that not only full prototypes but very early prototypes, prototypes of subsystems, breadboard and brassboard systems, all of this, is a plausible field for endeavor at the front end of the acquisition process when one has an opportunity to experiment with hardware and sometimes with simulations in order to help decide what one wants to do.

Our focus was very much to get more, in a sense, duplication, competition, activity into the front end of the acquisition system where failure is relatively inexpensive. I think it's not too far off to say that we were trying to help create a situation in which there might be more inter-service rivalry rather than less, more rivalry between the Defense Advanced Research Projects Agency's laboratories and contractors at a point in the process when failure is relatively inexpensive, when one is working with a few engineers, rather than later on when one is working with hundreds or thousands.

There are many excellent examples of cases in which work of this sort in the Department of Defense has paid off. Seventeen years ago this committee held hearings, which I did the staff work on, on the acquisition system, and one of the witnesses was the late Bill McLain, the inventor of the Sidewinder at China Lake. McLain invented what for many years was the only really successful air-to-air missile. He did it with a few people in a hangar on the side, and then the thing failed well over 20 times when he first began his work on it. But the failure was inexpensive. You had a genius who came up with an idea that other people hadn't really thought of, and in time he got the system to work.

So one of the things that we were trying to do was to get various parts of industry and the Government, in a sense, acting more like Bill McLain. Some such efforts are going to pan out, as his did; others will not. But where one is free to experiment, rather than be locked into rigid requirements, one can learn a lot from it.

Chairman NUNN. Thank you. Senator Thurmond.

Senator THURMOND. Thank you very much, Mr. Chairman.

Mr. Packard, we are very pleased to have you here. You have rendered long and capable and distinguished service to our country over the years, and we appreciate it.

Have you had an opportunity to be briefed on the recent efforts of the Under Secretary of Defense for Acquisition, and if so, what is your opinion? And could you be as brief as you can?

Mr. PACKARD. I have had a chance to get a reasonably good feeling about how things are going in his job. I referred to this in my testimony. I attended a meeting down at Fort Belvoir just last week in which he planned the program, and I think he is moving ahead well.

This job that he has is a very big job, and I think it is not reasonable to expect somebody to come in and get everything straightened out right away. I think he is making very good progress.

And I think, as a matter of fact, it would be a very desirable thing if you could get some continuity in this assignment to carry on between administrations. This whole issue should not be a partisan issue; it ought to be an issue of how we're going to get a better defense capability for our country.

And while we had a little difficulty in the beginning on the selection of this individual, I think, as you know, we're about as well off as we expected to be.

Senator THURMOND. Thank you very much. I presume by what you said that you favor long-term continuity in this position.

Mr. PACKARD. Well, continuity is a very important thing. That is the issue we have talked about in terms of the funding because if you have a program started and you have it halfway done and then change your mind, that's the best way to waste a lot of money. And I think the same thing is true of some of our fundamental policies.

Maybe partly as a result of the commission's recommendations, and certainly as a result of the work this committee has done, you have a lot of things going in the right direction now. They are not all where they should be, and I think it is very desirable to keep these things going with some continuity through the change of administration. That way we have a chance to really end up with some progress.

Senator THURMOND. Thank you very much.

Mr. Woolsey, we appreciate your presence and the fine service you have rendered to this country.

Very briefly, what are your thoughts on this subject?

Mr. WOOLSEY. I think Secretary Costello and Secretary Carlucci are getting started with some very positive steps here, Senator Thurmond. I think that trying to move away from such heavy reliance on fixed-price development contracting, trying to move toward a focusing—as under the CRAG program, as I mentioned in my testimony—of oversight resources on where problem areas are rather than distributing them generally across the whole world of the contractors is a positive step.

I think that Secretary Costello's background in industry equips him very well to move out, as he has begun to, on trying to utilize more acquisition of commercially available components and even systems, where those exist.

I suppose my only criticism would be that I wish this had started a couple of years ago. I think it is getting going now under Secretaries Carlucci and Costello, and I look forward, at least over the next several months, to seeing them continue to work with those of you in the Congress on the ideas that they have now begun to implement.

Senator THURMOND. Mr. Woolsey, Mr. Packard has taken the Congress somewhat to task, and a great many people feel as he does about Congress regulating itself. Do you have any thoughts on that subject?

Mr. WOOLSEY. Well, I think there have been a number of good and bad things that have come out of the Congress on these issues, Senator Thurmond. I think that it would be very beneficial if both the Congress and the Office of the Secretary of Defense could lighten up considerably on detailed management of the early portion of the acquisition system. I think we have altogether too many

DSARC's and program reviews and briefings during the period in which technology is being experimented with and concepts are being formulated before a decision is made to go into full-scale engineering development on a system.

I think if the Congress could, over time, bring itself to utilize relatively general areas of appropriation and authorization for the front end of the process before a system enters full-scale engineering development, it would do a great deal of good. And it's not only the Congress; it's also the Defense Department.

A gentleman known to many of you here on the committee, retired Air Force General Glen Kent, who is normally thought of as principally an expert in strategic weapons issues, has done some excellent writing at the RAND Corporation in recent months on this subject of managing the front end of the acquisition system. And one of his favorite expressions is that, up until pretty late in the process, "the sign over the colonel's door should read 'interdiction of Soviet armor in Europe, not JSTARS'." In other words, what money ought to be appropriated for, and what ought to be reviewed at the level of congressional committees and the Office of the Secretary of Defense, should be operational concepts for executing military efforts, perhaps in a specific region, perhaps with a general type of capability—but not the thousands of line items with $1 million moved from this to that and $3.4 million moved from that to this that has often been the management style in the Congress and is almost always the case in OSD.

I think we need to free up the scientists and engineers and military users at the front end of the process to talk to one another, interact with one another, and experiment some. But then once you start employing a fair number of people on a program, once you get into the business of going into engineering development on it, then both the Congress and the Office of the Secretary of Defense should have a very thorough review.

Senator THURMOND. Thank you very much. I've got to go to another committee, and I have one more question for each of you.

Mr. Packard, one of the problems identified during the review of Department of Defense organization is that the offices of the service Secretaries often ignore guidelines by the Office of the Secretary of Defense or attempt to stonewall efforts to terminate programs. I believe General Bernie Rogers recommended we eliminate the service Secretary positions. Had you given any thought to this and what is your opinion about it? And Mr. Woolsey, I will ask you the same question in just a minute.

Mr. PACKARD. Well, Mr. Thurmond, I might say that when I was there we had some very good experiences with the service Secretaries. Senator Chafee and Senator Warner here worked very closely with us, and we didn't have all of those problems. So, I don't know that I would say that you ought to eliminate the service Secretaries.

But I think the service Secretaries should work more cooperatively with the Secretary than they have done in this administration.

Senator THURMOND. Mr. Woolsey.

Mr. WOOLSEY. I had the fortune to work for Graham Claytor when I was Under Secretary of the Navy, and he was Secretary. I think in many ways he was really a model of the way service Secretaries ought to operate. It is a unique position in government because in a sense it serves a kind of brokering role between the interests of the uniformed service and the policy guidance from the civilians in OSD and in the Congress.

I think when the job is done right, it is rather heavily focused on not only the traditional functions of a service Secretary—keeping the morale of the service up, showing the flag and so forth—but also on managing acquisition. But not in managing acquisition in a hands-on way of participating in the selection of which contractor is going to get a contract.

I think what is important for the service Secretary and his immediate subordinates is to ensure that the uniformed service implements the decisions of the Secretary of Defense, but at the same time that the Secretary of Defense and his staff know about and learn about those aspects of acquisition, and training, and manpower policies and all the rest of it that are unique to the uniformed service over which the service Secretary has been given responsibility. And that two-way communication frequently breaks down in the Defense Department unless a service Secretary is working it continuously and effectively.

Senator THURMOND. I wish to thank you gentlemen for your presence here.

Mr. PACKARD. Could I just add one comment to that point, Mr. Chairman? I have felt for a long time if you look at what it takes to make a winning team, no matter whether it's in athletics and business or in government, you can get the best players in the world on both teams, but unless you've got good teamwork, you're not going to have a good team. And I think that is something that we all ought to keep in mind. We can never have a good effort in this military acquisition unless we can develop and maintain a real sense of teamwork. There is no way to do it by getting a bunch of individual experts or prima donnas involved in the process. It takes good people. It takes teamwork, and it takes the will to win. Those elements are required no matter what you're doing if you want a winning team.

Chairman NUNN. Thank you.

Senator THURMOND. Thank you very much, Senator Nunn, Senator Warner. I wish to thank you all very much.

Chairman NUNN. Thank you, Senator Thurmond.

I believe Senator Bingaman, under the early bird rule, is next.

Senator BINGAMAN. Thank you, Mr. Chairman.

I'd like to ask a couple of questions on this best and final offer process, and I think both of you commented on it in your testimony. From what I can determine, the evidence seems to be developing that this is one of the fertile fields for the kind of corruption that is coming out in this current scandal. Secretary Carlucci has taken some steps to limit contractors to one best and final offer rather than the multiple best and final offers that we have had in place before.

My question is why even have one unless there is some change in the scope of the contract or something that is changed from the time the original bid was made. Why not just have the contractor make a bid and have the judgment made on the basis of what is proposed instead of going back to him and having this best and final offer thing? Why shouldn't we just eliminate the process entirely except where there is this change in what is being asked for?

Mr. **Packard**. Well, Senator Bingaman, I happen to think it would be better not to have any.

Our big problem here is that we are not able to measure what we're trying to evaluate as well as we would like. That is why I think it's very important to try and get some way of evaluating these things on a way you can actually measure them. That's why I think past performance should be given a much higher priority in selecting the winners.

The trouble is now that, sure, if somebody at the last minute comes up with a much better idea, you ought to leave a little option to do that. But just ask everybody to go back when a lot of the stuff they're proposing is just paperwork, brochuremanship of what they're going to do and not necessarily anything very accurate in the way of prediction. I think we would be better off to put a high rating on past performance and a high rating on a number of things that would involve whether the contractor currently has the right ability or not to do the job, and then get the bids in and let the cards fall where they will and not go back and try to keep getting them refined. All that does is just ask for trouble.

Senator **Bingaman**. Mr. Woolsey, did you have a comment on that?

Mr. **Woolsey**. I would say, Senator Bingaman, the main reason it is done is to get the price lower. It does leave open the possibility of corruption, but I think it ought to be clear that probably, for many as years as BAFOs, or best and final offers, have been used, contracting officers have either directly or indirectly in many cases let competitors know what all others are bidding and have frequently let all competitors know what all other competitors are bidding in order to try to encourage everybody to get the price down. Sometimes they do it verbally. Sometimes they might leave a paper lying around their desk when a contractor comes in to visit them.

A contracting officer gets credit for getting the price down. One way he can get the price down is by that sort of leveling, and it accrues to his benefit and to the benefit of the Treasury.

Consequently, there have been a number of people who have advocated the BAFO, and some aspects of it are encouraged in the Competition in Contracting Act. But there have been people who have very much gone overboard with it. Multiple BAFOs do create serious problems.

I would think whether to permit best and finals at all is something that this committee would want to look at carefully and have a specilized small hearing on. I think it is a perfectly worthwhile area of investigation.

Senator **Bingaman**. Is there also a problem with what is called technical leveling in that everybody essentially knows what everyone else is bidding at the time of the best and final offer, and everyone has a tendency to essentially bring down what they are proposing to the least common denominator technically? Is that part of what goes on as well?

Mr. **Woolsey**. It certainly happens, yes.

Senator **Bingaman**. Let me ask about another comment that you make in your testimony, Mr. Woolsey. You say it may be that the committee should look hard at the use of consultants in source selection although other uses of consultants seem to be essential to the operation of the system.

Are you saying that possibly we should prohibit the use of consultants by the services in source selection?

Mr. **Woolsey**. I think it might be something the committee would want to do. Again, after hearing some of the reasons for it in the past, it's my understanding that some of the services do this more than others. It may be a historical matter related to cuts in acquisition personnel in the past and the details of highly complex RFPs that need to be put together for such things as ships.

I would think you would need a pretty careful look from the three Service Acquisition Executives about what they've done in the past, what the history is of the use of consultants in source selection—putting together RFP's and so on—and what changes they could reasonably make over time.

But it is one of those areas, like multiple best and final offers, that seems to me to create a potential for corruption. It is not the case that one wants to come out generally against the use of consultants either by private companies or by the Department of Defense. I think the consultant problem, at least so far, looks to me as if it has cropped up in this specific area, and so this would seem to me to be the area to focus on.

Chairman **Nunn**. Senator Bingaman, thank you.

Senator **Bingaman**. Thank you very much.

Chairman **Nunn**. We have a 15-minute rollcall. If some of our members can go ahead, I will wait here as long as possible, and we will then start the hearing as soon as someone gets back. I will stay here at least until the 5-minute bell, and we may take a brief recess. But that way we will minimize the time.

Senator Warner.

Senator **Warner**. Thank you, Mr. Chairman.

First, an observation. We are very grateful for these two fine persons to come in here and give us the benefit of their many years of expertise. I think it has been a contribution to this process.

I'd like to, in my opinion, describe the process that we are going through at this time with this committee. We are performing what I call the regular oversight of the procurement process (and this hearing serves that purpose) as well as trying to probe in such a way as not to interfere with the investigation of the current alleged scandal in the Pentagon. So, it seems to me to be a parallel track that the chairman and I have discussed.

Now, to the second point—the alleged scandal—in my judgment I think that this committee and other Members of Congress would be well advised to wait until the facts are out on the table as to what did happen, what is proven in terms of a body of fact before we try and react to that situation.

To the extent that I have had an opportunity to look at it, largely through these hearings, the alleged problem seems to be concentrated in just one military department, the Department of the Navy, with a small amount alleged to have occurred in the Department of the Air Force, and in our last inquiry, very little or nothing in the Department of the Army. This confirms the belief that I have held that 99.99 percent of this system in terms of the people in it, both uniformed and civilian, as well as contractors and consultants on the outside, are going about their business in an honest manner and trying to do the very best they can to make it work.

Now, one of the things that has come to the forefront again in this alleged controversy and which we must address once again by the committee is the revolving door and should we in any way try and change the rules that we put on here a few years ago.

I would like to have Mr. Packard lead off because, Dave, you referred—and I will call you Dave just for a minute—to the teamwork. Well, I remember the Laird-Packard team which I was privileged to be a subordinate in, and we did have teamwork there. It was largely due to the forceful personalities of Secretary of Defense Melvin Laird and yourself. You brought us together, the service Secretaries and the principal Assistant Secretaries of Defense, and you knocked heads. We worked together as a team, and frankly we played together. We used to go off on conferences and work hard. We got to know each other very well. It was the trusting and respectful relationships that contributed to the work on that team.

But let's go back to this question of the revolving door, Mr. Packard, because you've observed it for these 40 plus years that you have been in industry, and then you came from industry through the revolving door I suppose into the Department of Defense and out of the revolving door back to your firm again. And no one has ever laid a finger on you nor will they with respect to conflict of interest in the performance of those duties.

What could you advise us with respect to the revolving door and what we should or should not do at this time?

Mr. Packard. Senator Warner, you may note in my statement that I mentioned the revolving door as being one of the issues that relates to, of course, the manpower—getting the right kind of people into the Department. But I didn't make any further comment about it.

I guess in simple terms, I don't think it is as big an issue as a lot of people make out of it. If I look at it from my own vantage point, it would be very desirable to have broader access to people who have experience and who could come out here and utilize that experience and go back and do something else.

On the other hand, you've got to look at the realities of the situation. This is a political world, and you can't do some things you can do in the private sector.

I look at my own experience, and probably the thing that helped me more than anything else was the fact that I gave up quite a bit in terms of my ownership in the company to be able to come out here, and not many people would be willing to pay that high a price.

I think the revolving door has to continue to be an issue. You can't eliminate the problem. I don't think you can do very much different than you are doing. You have to have some rules. They shouldn't be too tough. And we ought to have an opportunity to get some better people in. But you have a problem of public perception. You have a problem of politics, and I don't think there's a very simple answer to the revolving door issue.

Senator **Warner**. Mr. Packard, I'll have to go vote, and I'll be right back. And then I'd like to have Mr. Woolsey address the question.

[Recess.]

Senator **Exon** [presiding]. The committee will please come back to order. I've been asked to proceed.

I believe Senator Warner has a little time left. According to the early bird rule, the Senator from Illinois is next. And I'll be glad to recognize him at this time. Senator Dixon.

Senator **Dixon**. I thank you very much, Mr. Chairman.

I would like to observe at the outset that both Mr. Packard and Mr. Woolsey have certainly made very substantial contributions in the view of this Senator and I think the entire Armed Services Committee to the very significant improvements that in my view have been made in acquisition and procurement in recent years. As a sponsor of the amendment to the DOD reorganization bill that set up the Under Secretary of Defense for Acquisition, I want to thank you both for your very firm support which was critical to the passage of that legislation.

I guess having said all that, Mr. Packard, I would want to underline on page 10 of your statement when you say—and I quote you directly—"I told them that the commission intended to give them the message that there should be only one chain of command in acquisition, and apparently they did not get the message."

I would have to observe, before I ask you the question, that throughout this evolutionary experience, since we passed the Under Secretary of Defense for Acquisition legislation, I remember the breakfast that some of us as Senators had with Mr. Godwin. I remember when Mr. Godwin resigned and when he came here. I think Dr. Costello has demonstrated he can work inside the system better, but I would want to observe that I think that a lot of people there still have not gotten your message, sir.

Mr. **Packard**. Well, we asked the Department to make some rather fundamental changes. And I think no one expected those would have been done easily or quickly.

That is an issue that we just simply have to keep working on. I still think that our efforts in that area are going in the right direction. I think we ought to continue it. We should not be discouraged by the fact that we haven't accomplished as much as we had perhaps hoped. But let's don't assume that that means what we're doing is not the right way to go. I still think it is.

Senator **Dixon**. Well, I respect your views and agree with them.

I would ask you respectfully to look at S. 2621, a bill I've introduced which continues to try to further strengthen and centralize the authority and establish the chain of command under the acquisition chief in the Department of Defense. And I would very much appreciate the critiques of you and Mr. Woolsey for that legislation.

I have here, Mr. Packard and Mr. Woolsey, Inside the Pentagon from July 8. I don't, incidentally, agree with Dr. Costello if he was trying to stop the B-2 advanced tactical bomber program. I think we need it. But I think there's a lot of problems in it.

But I think page 3 of Inside the Pentagon on July 8 makes it pretty clear that Dr. Costello still does not have the authority we would intend for him to have by virtue of what transpired there. I'm not going to quote at length, but I think clearly the service Acquisition Chiefs and others still have significant power to play their own individual games in the system to the, in my view, detriment of the system. I'd like to have the comments of both of you on that.

Mr. PACKARD. Well, I think you're correct about that, that this office and the person in it is not yet as able to exert as much authority as we would like to have.

Now, you know I'm sure that you can set up procedures that will dictate a person has authority. That doesn't necessarily give him that authority.

Senator DIXON. Yes, sir.

Mr. PACKARD. I remember a very interesting case we had in our company very early on. I appointed someone to be the manager of a department, and after a little while he asked me to come out there and tell everybody that he was the manager of the department. And I said if I have to do that, you're not the manager. [Laughter.]

I think that's the kind of a problem you have over here.

Senator DIXON. You know you made reference—and I'm glad you did—to the Wall Street Journal of Tuesday, July 26, 1988, the article, "Paris Cuts Costs, Limits Corruptions in Arms Purchasing." It talks about a few things—and I'm not advocating adopting the French system, but I just wanted to quote:

> One of the key problems in the United States, investigators say, is that the separate buying arms of the U.S. Army, Navy and Air Force results in costly duplication of development, bad coordination of purchasing and invites corruption when officials move between government and private industry.

It goes on to point out—and I quote directly—

> The French acquisition agency, created against the wishes of the French military in 1961 by General DeGaulle, is directly answerable to the Defense Minister, a civilian appointed by the Prime Minister, not to individual service chiefs. The DGA sifts requests for new weapons from each service, places orders for them with the companies and controls both price and quality.
>
> All three French services a few years ago wanted to design and develop their own surface-to-air missile. The DGA decided they would all get the same one, and they designed the missile.

Well, I just want to point out that to that extent I think the article demonstrates what I have said here for a long time echoing, Mr. Packard, what you and Mr. Woolsey have said—that a centralized system that manages procurement and acquisition would avoid duplication, save money and in many ways better serve our national security interests.

Mr. PACKARD. If you look at the structural changes that have been made, the things we talked about in our commission and the things this committee has supported, you now have established a structure to do essentially what you're talking about. And it's going to take some time to get it done.

I think it is very important for everyone involved here, particularly this committee, to continue pushing on that. You have the structure set up so that the Chairman, the Vice Chairman and the Under Secretary for Acquisition are supposed to have the final determination on what weapons are to be bought from recommendations of these services. I think if we keep working toward that objective, we're going to get where we should be.

I think we have got a good start in it. I saw that article, and I don't think we need to do anything more than keep going the way we have started. We will get where we ought to be.

Senator DIXON. Thank you.

Mr. Chairman, may I have one final question?

Senator EXON. Yes, and we will then go back to Senator Warner.

Senator DIXON. Thank you, Mr. Chairman.

I just want to comment to Mr. Woolsey that I was intrigued very much by your closing comments on page 9 of your statement where you say, "It may require moving toward the development of civil remedies for use to discipline wrongdoers where appropriate rather than relying solely on the more drastic ones of the criminal law, debarment and suspension."

I wanted to urge you as well to look S. 2621. My bill does two things. It centralizes even further the acquisition and procurement process. But then it sets up standards of conduct for procurement officers inside the system and the defense industry and gives civil remedies that would act more quickly. You would only have to use the preponderance of the evidence instead of beyond a reasonable doubt. A lot of things could be done structurally more swiftly and in the interest of the Government and the taxpayer.

I'm indebted to you for your statement because I think it reflects the inside understanding by you and others of how this system could be improved. And I would very much like your comments on that portion of my S. 2621.

Mr. WOOLSEY. I'd be delighted to comment, Senator Dixon.

Senator DIXON. I thank the Chair.

Mr. Chairman, could I have these statements in the record?

Senator EXON. Without objection, so ordered.

[The information follows:]

[From Inside the Pentagon, July 8, 1988]

B-2 PASSES DRB REVIEW DESPITE COSTELLO'S MOVE TO KILL PROGRAM

The high-profile, classified near-$60-billion B-2 Advanced Tactical Bomber (ATB) has passed a major review by the top-level Defense Resources Board, despite efforts by DOD Undersecretary for Acquisition (USDA) Robert Costello to terminate the program, Pentagon officials say. Specific funding levels for ATB are classified, DOD sources say. The ATB is the Air Force's next generation stealth bomber with a total program cost estimated at $59.5-billion.

Pentagon officials say that Costello proposed killing the B-2 program during the DRB's closed session last week on "special access programs." But Costello's proposal was not supported by other key DRB officials, including DRB chairman Deputy Defense Secretary William Taft.

Costello's concerns regarding B-2 reportedly center on alleged "mismanagement" of the program as well as current fiscal constraints on the defense budget (Inside the Pentagon, June 17, p. 1). Costello earlier argued that ATB costs could be cut by as much as $18-billion by subjecting the program to his new "could cost" acquisition strategy. But concerns about possible Northrop mismanagement of the program led Costello to recommend the ATB be terminated.

Sources say that DOD officials attending the closed DRB session agreed that program costs for B-2 must somehow be decreased. Costello reportedly will continue to work with Northrop to apply the "could cost" acquisition strategy to drive down the program's cost. Could cost is explained by Office of Secretary of Defense (OSD) sources as a system for determining a program's cost based on minimizing the non-value-added work done by a contractor. Sources say it will cut costs associated with the 40% of DOD programs presently being conducted under sole-source arrangements. Other programs selected by OSD as "model" could cost projects include the Army's AH-64 Apache helicopter, the Marine Corps' V-22 Osprey tiltrotor, and the Navy's Trident D-5 submarine.

[From the Wall Street Journal, July 26, 1988]

Paris Cuts Costs, Limits Corruption in Arms Purchasing

WASHINGTON IS LOOKING TO LEARN IF FRANCE'S SYSTEM IS WORTH ADOPTING

(By Philip Revzin)

Paris.—The military men who work in the left-bank offices of the Delegation Generale Pour l'Armement, or DGA, all have uniforms. But significantly those uniforms aren't the same as those worn in the French army, navy or air force.

That is because the DGA which is responsible for weapons development and procurement for all three French services, totaling about $15 billion a year, is part of none of them. That, say the French, makes toute la difference.

The French system of supplying arms to its armed forces is being seriously studied in Washington as a possible basis for reform of the Pentagon's scandal-plagued weapons procurement system. One of the key problems in the U.S., investigators say, is that the separate buying arms of the U.S. Army, Navy and Air Force results in costly duplication of development, bad coordination of purchasing, and invites corruption when officials move between a government and private industry.

The French avoid many of the problems by centralizing control in the DGA, run by a corp of military officers who are also professional, career arms designers and buyers trained to understand both the mechanics of weapons systems and the politics of the armed services.

In Washington, the House Armed Services Committee plans to hold hearings this fall on proposals to replace the tri-service buying bureaucracies with a French-style professional acquisition crops. A measure introduced by Rep. Dennis M. Hertel (D., Mich.) would staff a Pentagon agency, similar to the DGA, with officers who are career acquisition specialists.

"There is genuine agreement that we have to 'professionalize' the acquisition system," says an aide to the House committee. "Obviously the French model is one where this works successfully."

A more drastic measure sponsored by Rep. Barbara Boxer (D., Calif.) would remove the military from the acquisition process, turning responsibility for designing and testing weapons to a new agency staffed by civilians. The Pentagon is expected to oppose such a measure.

A French acquisition agency, created against the wishes of the French military in 1961 by Gen. Charles De Gaulle, is directly answerable to the defense minister, a civilian appointed by the prime minister, not to individual service chiefs. Its 1,000 military officers supervise a staff of 25,000 mainly civil servants, who act as a buffer between the military services and the arms producers, which in France are about evenly divided between state-controlled and private firms.

The DAG sifts requests for new weapons from each service, places orders for them with the companies, and controls both price and quality. All three French services a few years ago wanted to design and develop their own surface-to-air missiles. The DGA decided they would all get the same one, and got Matra S.A. to design the Mistral missile. When French industry suggested developing its own early-warning surveillance aircraft, the DGA found the idea too costly, and recommended buying U.S.-built Awacs planes instead.

The DGA is currently deciding how many different versions of Avions Marcel Dassault's new Rafale fighter should be produced, in response to requests for five different models from the air force and navy. The DGA also keeps close tabs on equipment costs. Because of this, says a Defense Ministry official, the French Mirage 2000 fighter program came in on budget while the rival European Tornado fighter was 25 percent over budget. "Whenever the air force or navy would come and say they had 20 new specifications to add to the plane, the DGA told them to forget it," the official recalls.

"The system certainly works well for them" says a U.S. military official. "Whether it would work in our much larger and much more complex system is an open question, though an interesting one."

Francois Heisbourg, director of the International Institute for Strategic Studies in London and a former French arms industry official, says a U.S. version of the DGA would require replacement of the Pentagon's procurement staff. That, he says, "would be fought tooth and nail by the joint chiefs, and also by Congress, which exercises a micromanagement of the Pentagon that the French parliament doesn't come close to."

"The key thing is that the people [in the DGA] run no career risks by making decisions one particular branch of the military doesn't like," adds Mr. Heisbourg. "They are inter-service and inter-service all their lives and so have no fear of saying no to a new tank and going back to the army three years later to face a firing squad." He says the system enables the inevitable inter-service struggle to be played out far from the public eye, and for the occasional cancellation of weapons systems before development costs run amok.

DGA isn't problem-free. It is staffed mainly by bureaucrats, carefully trained in the rigid French system, with no experience of managing a company. Arms companies sometimes complain that DGA bureaucrats make unreasonable demands. The services, and potential foreign buyers of French weapons, complain that the DGA-directed system has killed competition among French companies—only one makes planes, another makes rockets—which sometimes lead to sloppy, unimaginative products. While the Pentagon uses a sophisticated French battlefield communications system, Dassult is having trouble selling its new jet fighter outside France.

Another problem, members of parliament say, is that the power concentrated in the DGA takes a strong defense minister to control. But DGA officers contend that if they abuse their authority, the defense contractors and the individual services complain loudly to the minister.

The cosiness of the system, requiring close cooperation among the services the DGA and the arms makers, does invite revolving-door movement between the government and industry. But because much of the arms industry is state-run, and because salaries in both sectors are similar, there is probably less temptation to corruption, the French say.

"No system is perfect, but we've probably got more efficiency and less corruption because of the DGA," says a former top DGA man. That doesn't mean there aren't scandals, but these involve breakdowns in the control over arms exports, for example to Iran or South Africa.

"The fact that France has had the DGA," says the former DGA official, "has enabled us as a medium-size country with a limited defense budget to develop a coherent, effective, efficient, nuclear and conventional defense industry second only to the U.S. within the Western alliance. If we had wasted our resources for the past 25 years we would never have been able to do it."

Senator **Exon**. I think it is proper we go back now to Senator Warner to complete his questions that were interrupted by the vote.

Chairman **Nunn** (resumes Chair). Senator Warner.

Senator **Warner**. I thank the courtesy of my good friend from Nebraska, Mr. Chairman.

And the question on the revolving door had shifted to Mr. Woolsey. If I can repeat for the record, you yourself are part of the revolving door. You came from the private sector, went to the Department of Defense, served with distinction, returned to the private sector. Who knows, you may go back to that Department of Defense willingly or unwillingly some day——

[Laughter.]

Senator **Warner** [continuing]. Because you have established yourself as a defense expert and with unquestioned credentials.

Mr. **Woolsey**. Thank you for those kind words, Senator Warner.

I think that the revolving door problem is a complicated one. I think it's important to realize that in 1978 and 1979 some major changes were made in title 18, section 207, the post-Government employment conflict of interest. And those restrictions place some fairly important constraints on what an individual may do after he leaves Government with respect to communicating back to the executive branch or otherwise representing a client or a company with which he had been directly and or indirectly involved when he was inside the Government.

Those are new restrictions and people are only now fully beginning to come to terms with them because they are somewhat complex. There are certain things you can't do for the rest of your life. There are certain things you can do after a 2-year period. There are certain things you can do after a 1-year period. But all of the restrictions in section 207 have to do with communications with the Government.

Now, a couple of years ago the Congress passed some further revolving door legislation which restricts employment effectively for Government employees who have spent a very substantial share of their time working on acquisition or on a particular program in certain ways. It was that legislation which was coming into effect just before some of the individuals who were involved in the current procurement investigation left the Government. So, it is not clear whether or not that legislation would have effectively restricted some of the activity that has taken place.

I think that it is important for the Congress as it looks at the revolving door question to keep in mind that it does have to be doing some balancing. It can realistically, as it did in 1978 and 1979, put restrictions on an individual's communication with an intent to influence the Government, his communications back to the Government after he leaves. I believe it is realistic to place the kinds of restrictions that were placed a couple of years ago with respect to some individuals' employment.

But if one goes further and makes it virtually impossible for those who work in Government to leave and to go out and earn a living even in a general area of their competence, then by choking off the possibility of leaving Government and working in the private sector—since these individuals can read and understand what the future will bring—one is also going to severely restrict the ability to bring people in from the private sector into Government.

Senator **Warner**. Of quality.

Mr. **Woolsey**. People of quality.

Senator **Warner**. So, what's the bottom line here because my time has run out? Leave it the way it is at the moment?

Mr. **Woolsey**. I would for the time being certainly not pass any further revolving door legislation. I would monitor what has taken place so far and see how the legislation that it is already passed either was violated or might have, had it been in effect on the relevant date, restricted the activities of some of the individuals once all of the facts are known here.

But I would urge the Congress not to pass further revolving door legislation right now. It is hard enough to get able political appointees, in. There is, as Dave has pointed out already, and I agree, an excess of lawyers in the process. I think one wants to make it possible for engineers and people who have walked the shop floor and made cost and schedule and performance all work out appropriately in program—one wants to make it possible for individuals like that from industry to serve in the Department of Defense in acquisition.

Senator **Warner**. Mr. Woolsey, I have your answer and I concur with it and I concur with that from Mr. Packard.

You were about to say something else, Mr. Packard?

Mr. Packard. Well, no, except I would just like to make one clarifying statement about lawyers. I have no objection to lawyers who really know what they are doing in this business. And in deference to my friend here, I want that to be understood.

Senator Warner. Would the chairman and my good friend from Ohio indulge in one little reminiscence that will take 10 seconds——

Chairman Nunn. Go right ahead.

Senator Warner [continuing]. Because it brought back a memory I had when I was Secretary of the Navy?

Someone referred to me, as you've just referred to Graham Claytor, as a model Secretary of the Navy. I thought it was pretty good. I liked it. And I went home that night and my daughter, who was with me said, "Dad, I'm troubled by that comment that was made." She overheard it. And I said, "What troubles you?" She said, "Well, just look in the dictionary. The definition of "model" is a drastically reduced version of the real thing." [Laughter.]

So, knowing Graham Claytor and his tremendous capabilities, perhaps you had better select another——

Mr. Woolsey. I meant what you at first thought was meant about you, Mr. Chairman. [Laughter.]

Chairman Nunn. Thank you, Senator Warner.

Senator Glenn.

Senator Glenn. Thank you very much.

I wanted to follow up a little bit on the remarks Mr. Woolsey made on functional budgeting. Suppose we have a colonel that's in charge of ASW whatever it is, whether it's air, surface or subsurface ASW because I've talked for years, and years about the value of net assessment to determine requirements as opposed to everybody running off doing their own weapon system development.

I don't like what, for lack of a better word, we call the Time magazine approach to this thing where we list these weapon systems and the Soviets have so many bombers, we have so many bombers. We're behind. We obviously need more bombers. Well, the facts are that bombers don't go out and fight bombers. We have a lot of ways of delivering explosives or whatever they are on the enemy, and they have a lot of ways of countering that and vice versa.

DARPA, for instance, uses to some extent the approach that you're taking about of ASW which comes under one shop, and they develop whatever it is anti-sub, air, attack submarines, and do the ASW technology out of one shop there that coordinates the whole problem.

Obviously, the next bottom line would then be you take all the defensive things and you take anti-tank in one shop, anti-sub, anti-air, whatever, in the offense, and you break then down the same way.

Are we remiss in not insisting that that kind of organization reflect what is our overall objective anyway which is combat capability? That's all we have a Defense Department for is combat capability. And that comes as net assessment takes hold in combat. Should our procurement system be organized along that same way like right back from combat? Or is that too much to ask for?

Mr. **Packard**. Well, I think you have made a very important point here. Obviously, if we don't have a unified strategy, if we don't know what we're trying to do, how can we possibly select an optimum mix of weapons?

Now, if you look at what has happened over the past few years, our strategy has been driven by our concern about the possibility of a Soviet threat to the central front in Europe by the possibility of a nuclear exchange. And really, the confrontation between the United States and the Soviet Union has been an important driving force in what both we and they do in development of weapons.

Now, we are finding, it seems to me, that there are some other problems. I felt for a long time, if you look at the probability of these things happening, the probability of the Soviet thrust through the central front is fairly low. You can make a list of the weapons they have, the number of tanks, the number of long-range artillery pieces and so forth. You can make a good case that that's what they are planning to do.

But if you look at the situation a little further, the fact that they're going through rather hostile territory and what value that would have and so forth—and I think we have not really thought through what we really should be trying to achieve as well as we should. That is, of course, one of the reasons we keep talking about let's get out of this detailed, line item consideration by the committees here and pay some attention to these bigger issues.

Senator **Glenn**. Well, in effect, that is what you would be doing if you went to functional procurement that reflects what you want which is combat capability.

Mr. Woolsey, do you——

Mr. **Packard**. Well, let me just add one other comment to that. I think this is a much more important issue right now than it has been in the past. It seems to me there is a very great probability that there is going to be some change in the confrontation between the United States and the Soviet Union, but to think that we're going to get rid of conflict and contention in the world is unrealistic. We really must think through what kind of capability we are likely to need for these issues we are going to be dealing with 10 and 20 years from now because that is what our present decisions are all about. This issue is more important even than I thought it was 2 years ago when we talked about it in the commission.

Mr. **Woolsey**. Senator Glenn, I completely agree. This principle of organizing back from combat, organizing essentially your own early R&D efforts around what you're trying to accomplish as distinct from organizing around your own platforms, is a crucial aspect. And I think very few things could improve the front end of the acquisition system more and very few things could do more to give us a better handle on what technology what would be available to us than trying to free up and loosen up on that early part of the acquisition cycle, letting it be handled generally within some of these mission areas. Having a close cooperative working relationship between military users and technical people at that stage is essential. It is very much in line with what we recommended on the commission.

I would urge you again to have a look at what Glen Kent has been doing at the RAND Corporation precisely on this point.

Senator **Glenn**. If we went that route, it would be an enormous change in defense procurement.

One other area here, Mr. Chairman, if I might. Mr. Woolsey, in your statement on page 7 you said, "There is no doubt we need fewer people in acquisition, but it needs to be fewer reviewers, advocates, inspectors and people who liked to be briefed. So, this transition needs to be managed by incentives to make the system and the personnel slots evolve in a proper way." If the answer is that we have too many people and not the right people over there, then do we need to go more in the acquisition process to czars or to program directors that actually have authority to do things? And if so, then what do you do? Do you have a stronger IG set up to monitor what they are doing as a backup on it?

And let me just say this. In the Governmental Affairs Committee that Senator Nunn and I are both on, that I chair, some 10 years ago we were fundamentally involved with putting together the whole IG system. Now, we did it with sort of a question mark. Would it be of any benefit or not?

You get the IGs up here now and we literally have saved tens upon tens of billions of dollars through the IG system and checking and ferreting things out before they get to the great national scandal level. And I think it has been very good.

Now, if we went to the fewer people and a czar type management, something like SDI has now, as a real director, then would that be a good system where we give people real, honest-to-goodness program authority, but an IG system then to ferret any wrongdoing early on?

Mr. **Woolsey**. Senator Glenn, I think something very much like that is a good idea. In this special report for the Packard Commission that we put out in April of 1986, The Formula for Action, by the task force that Bill Perry chaired and that Dave and I were on, we start out by describing acquisition programs that work. And there are some, of course, in DOD. There are some in the intelligence community, the so-called black programs. There are some in private industry. They all tend to center around the strong program manager with the ability to trade off cost, schedule, and performance.

In essence, the effort of a lot of what we recommended was to try to make more of the Department of Defense acquisition system modeled after these programs that worked well. They are in many ways very close to what you were describing.

Now, if you're going to give people clear-cut authority and not be looking over their shoulder every minute with an advocate for this and a review board for that, you have to have some way of monitoring whether or not anything is being done illegally. And I think the IGs in the Defense Department do a good job.

The model that I suggested in my statement for monitoring the defense industry as a whole—whether or not time cards are filled out correctly, whether or not overhead is allocated properly as between fixed-price and cost plus contracts and so on—is the model of the Securities and Exchange Commission supervising, in a sense, the accurate financial reporting of American publicly-owned companies. They do it without having auditors and inspectors in every board room. They do it with selective enforcement, but they do it very well.

If we could, for the IG's and some aspects of what the Department of Justice does, model the compliance and enforcement mechanisms for the record keeping and the details of management of the Department of Defense's acquisition system more along the lines of the way the SEC monitors financial reporting by publicly-owned companies, then we would really have something that used fewer people and did a much more effective job.

Senator **GLENN**. My time is up, Mr. Chairman. I would just say I hope that, on my first line of questioning here on this combat capability net assessment in making our procurement system come right back from combat and reflect that as much as possible, we as a committee could look into that a little bit more because that's a very fruitful area. We have a tremendous amount of waste because we don't do that. And that's all we're here for is to make sure we have a good defense capability, combat capability.

Chairman **NUNN**. We've tried to move our committee in that way by having mission-oriented subcommittees rather than the other way around. We have tried to focus on the broader picture. As you know, we had I think 25 or 30 hearings on military strategy last year. That was when we started this 2 year period and it was looking at the strategy or the lack thereof. And so, I would certainly agree with that approach.

If I could interject here, and then I will call on Senator McCain.

I believe what you are saying about the SEC model is perhaps not too far removed from what Chuck Bowsher testified to in terms of having accountants that do the work for the companies and CPAs have a different standard of reporting so that you do not have to duplicate everything the internal CPAs do with external Pentagon-type auditors and CPAs.

But there is, it seems to me, a difference in what the SEC's role is and what the defense auditor's role is. The SEC reports, as I view them, make sure that the stockholders are given adequate information by which to judge the management performance. Defense auditors are trying to determine if defense contractors are cheating the customer. It seems that they are two different things. I'm not sure how you blend those two together because the stockholders can theoretically be well served in the short run if the customer is being cheated. In the long run I think it is very detrimental to everybody.

Mr. **WOOLSEY**. In the long run, it is.

Mr. Chairman, I agree that it is parallel in some ways with some of the things that Mr. Bowsher has suggested. In his testimony before Congress on July 11—and I confess, since I don't have a cover page here, I don't know what committee—this may have been before House Government Affairs—he talks about some new efforts at the SEC to begin to look at its assessment of the effectiveness of management's internal controls. He suggests that since the SEC principally focuses on corporate financial reporting and not on contract-specific data, which is your point, there would probably have to be some expansion of the role of the audit profession, the outside auditors, when they are looking at performance and at contract-specific record keeping by individual companies.

But I think although this is not well worked out yet, there is at least the germ of an interest in both the SEC and in the GAO in beginning—and I think it is very much in line with the contractor risk assessment guide program that Secretary Carlucci just announced a few days ago. There is a germ of an idea in two or three different places of using the Government's oversight capability with respect to contract-specific data in a rather more selective way along the lines—analogous and certainly not precisely the same—but along the lines of the way the SEC conducts its overview of financial reporting.

Clearly there are a lot of details to be worked out here. All I really meant to communicate was a general philosophy and an attitude.

Chairman NUNN. I agree with that general philosophy.

Senator McCain.

Senator McCAIN. Thank you, Mr. Chairman. I appreciate very much the testimony of both witnesses.

I would like to ask a couple of questions about a portion of Mr. Packard's testimony. On page 5, he says, "another devastating effect of the disgraceful congressional practice of funding programs for equipment that is not really needed by our military forces."

Mr. Woolsey, are you in agreement with that part of Mr. Packard's statement?

Mr. WOOLSEY. Well, Senator McCain, I followed only in the press some of the rather vigorous dialogue recently in the Senate on this subject with respect to the authorization bill. I think I would say that, in the 3 years I was General Counsel of this committee and in the years since in the Department of Defense and as a private citizen in following this, I've certainly seen a number of cases of programs being continued on and added to and conducted longer than was really necessary from the point of view of the Department of Defense.

On the other hand, on some of those cases I've thought that the congressional action was substantively more correct than the Defense Department's proposal to cut off programs or not go forward with them.

For example, when I was Under Secretary of the Navy, although I couldn't take a public role in it, I vigorously supported the AV-8B program. The Department of Defense tried to kill it every year, and the Congress kept it alive. I thought Congress was right on that and the Defense Department was wrong.

Senator McCAIN. Some of us also supported an additional aircraft carrier.

Mr. WOOLSEY. Yes, those things happen.

But we all know there are constituent pressures for some of these things to be kept alive and kept going longer than they should be.

My own overall judgment is that that happens a bit more in defense now than it did 15, 20 years ago, but it probably happens considerably less with regard to defense than it does to many other parts of the Government.

Senator McCAIN. I would suggest, Mr. Woolsey, that your statement is correct except in the fact that the pork doesn't come in on AV-8B's and aircraft carriers. It comes in on much smaller programs, much more minor, so-called line items that are passed without notice. Those are the areas that concern me, not whether there is a major philosophical difference as the one you pointed out.

Mr. **Woolsey**. I understand.

Senator **McCain**. I think that the only way we're going to address this area is, first, to have some kind of study done which can tell us exactly the extent of this problem, because that's unknown.

And second, I think I would like your comments on my view that we should expect the same standards of conduct from the legislative branch that we are demanding correctly from the executive branch. It is interesting to me that you, if you were a member of the Defense Department, couldn't accept lunch from a reporter here in this room, but I can accept an all expense paid trip with thousands of dollars of honoraria for myself and my wife to visit one of their facilities. That doesn't wash with the American people, and I would hope that both you and Mr. Packard would agree with me. I would like your comments as to whether we should expect the same standard of ethics out of the legislative branch as we are correctly seeking from the executive branch.

Mr. **Woolsey**. Senator McCain, if I were a czar on this sort of matter, I suppose I would do two things. One is that I would apply the same, or very close to the same, standards to the legislative branch that is applied to the executive branch and the judiciary branch but, on the other hand, I would also strongly support major increases in salary both for the executive Presidential appointees, the legislative branch and the judiciary.

I think part of the problem here that it is difficult as a Member of Congress to vote for salary increases for oneself, and it is difficult to have the executive branch make more than Members of Congress do. But it is also difficult over time as inflation erodes some of these salary levels for people realistically to contemplate public service for a long period of time without such things as taking honoraria for speeches and so on. I think that it is a tough problem.

Ideally I would like to see, I suppose, some of the same types of standards applied on the Hill as are applied to the executive branch, but I think it would also be a fine thing if across the board the salary levels of people who work for the Government could be increased.

Mr. **Packard**. I would support that too.

Senator **McCain**. Well, let me move on to the issue of multi-year procurement. I'm not sure how we achieve that insofar as we all know that you can't find future Congresses appropriating funds no matter what our plans and proposals are for this year. How do we get around that problem, Mr. Woolsey or Mr. Packard? We have an authorizing situation here where our chairman and the rest of this committee authorize multi-year procurement of certain pieces of equipment, yet we see those funds significantly change from year to year as a result of the appropriations process.

Mr. **Packard**. Well, I think we recognize that this committee and some of the people in the Congress have been pushing us in the right direction. And I will make a comment about the appropriations problem in here. Maybe I'm too facetious in saying that they are more interested in preserving their pork barrel opportunities than in doing the right thing here.

But I don't see how we can really get at these issues and have the time to do what needs to be done to look at the larger aspects of this problem unless we can go to a 2-year budget and more multi-year funding.

Now, I think it is necessary to recognize that multi-year funding is going to pose some difficult problems in the immediate future when it is not likely that there will be an opportunity for further real increases in the defense budget over the next several years. You already have more things in the mill than you are going to be able to fund so these multiyear programs tend to be counterproductive and you have committed so many dollars to that, and maybe in the out-years that is not the best thing to do.

So, you always get back to the fundamental proposition. You've just got to address all of these issues with a little more common sense. There are no simple answers to these things. They are complex issues.

Mr. Woolsey. Senator McCain, I think the only part I would add is that—although one shouldn't lock up so much of the defense budget in multiyear programs that you lose your flexibility—for stable programs, ones that are noncontroversial, ones that you know you're going to have to buy out over a long period of time, one can save a good deal of money with that type of stability. And insofar as Congress can do it with the cancellation charges and so forth in a way that doesn't violate the constitutional problem of one Congress not being able to commit another, I think the progress that has been made in that direction in the last few years is a positive thing.

I do think it would be a step in the right direction if we could move back with respect to the relationship between the authorizing and appropriating committees to something a little closer to that which used to exist in the early 1970s.

I recall then, although I don't know that this was the subject of any detailed memorandum of understanding between the committees, that effectively Armed Services dealt with the capital budget of the Department of Defense and Appropriations dealt with the operating budget. It was perhaps facilitated by the fact that Senator Stennis and other senior members of the committee at that time still served on both committees. So, the problem of having conflicts between the authorizing committees and the appropriating committees were easily ironed out.

But the appropriating committees in those days served a kind of comptroller function. They looked at contracts to make sure that when something had slipped and you only needed 11 months' worth of money, you could take out one-twelfth of the money. They looked at the operating budgets. There was some involvement with the hardware side, but not nearly as much as now. Armed Services only began in 1971 to authorize manpower, and in the subsequent years has it moved more into looking at broader parts of the operating budget of defense. Certainly it makes it easier to get a handle overall on the budget if one is looking at the whole budget.

But the problem now is that, since the budget committees look at the whole budget and the authorizing committees look at the whole budget and the appropriating committees look at the whole budget, in a way you go through the whole budget six times.

If there were some way to deal with the major capital issues in the authorizing committees, look at milestone authorizations and deal with the capital budget of DOD, and for the appropriating committees to deal more with the operating budget, and on those an annual look not only doesn't create a problem, it's a positive thing—one wants to do the comptroller type function annually—I think we would probably all be better off.

But I'm not sure that it is possible at this point under the Budget Act for Congress to get itself completely sorted out this way again. Perhaps I'm just looking back on the days when I was over here as a staff member and falsely remembering a rosy past that never really was.

Chairman NUNN. Well, we have three committees doing what I think at most two committees ought to be doing. And you can argue about which two committees, but there is no way that you can justify having three committees involved in all of that. Of course, the Budget Committee would contend they don't do anything but the broad macro, and to some extent that is accurate.

Senator McCAIN. Could I say, Mr. Chairman, a comment you made the other day that if we were in the days where you were serving on both committees a lot of the friction would be resolved rather rapidly. Although I think those were golden days that Mr. Woolsey is talking about, unless we change the rules to allow you to chair the Appropriations Committee, we're going to have——

Chairman NUNN. Yes, if you chair the Armed Services Committee and also the Defense Appropriations Subcommittee, the conflicts seem to iron out pretty well. [Laughter.]

Senator McCAIN. Thank you, Mr. Chairman.

Chairman NUNN. Thank you, Senator McCain.

Senator Exon.

Senator EXON. Mr. Chairman, thank you very much. I just want to add my salute to the two distinguished visitors and witnesses we have this morning, and thank you for calling them, Senator Nunn.

Certainly I want to take this public opportunity to thank you, Mr. Packard, as an individual who has been of tremendous help, more so than you probably realize, to those of us who have to deliberate and make these decisions.

And you, Jim, as a former staff member of this committee have been extremely helpful, and your participation in both the committee headed by Mr. Packard and the acquisition committee by our good friend Bill Perry has been of invaluable help. Your testimony has been excellent here this morning, and I have listened to it with great interest.

Many of the questions that I had intended to ask have already been asked.

After that big buildup of how confident we are of your recommendations, let me ask you something not directly on point with regard to this committee, but something that I think is on point with regard to the national defense issues of the United States. I would like to get your offhand opinions as to whether or not, as explained in the newspapers this morning, there is a move afoot to persuade the President of the United States to, indeed, veto the defense authorization bill that has been put together by many months of efforts on the part of this committee and culminated in consultation with the House counterparts in a knock-down-drag-out conference that we were recently involved in. It is my understanding that on both sides of the aisle the senior leadership of the Armed Services Committee is diametrically opposed to the President's veto for whatever reason. I'm wondering if you share the concerns of this Senator that if the President would veto this bill, it could become the unraveling of a constructive process that has taken a lot of time and effort. Do you have any opinions?

Mr. PACKARD. Well, Senator, I'm really not in a very good position to make an observation about that. I haven't seen the arguments. I haven't talked to anybody in the administration to know what the reasons are. So, I'm sorry. I can't give you any useful answer to that question. Jim, maybe you can.

Mr. WOOLSEY. Well, I guess maybe lawyers rush in where wise men fear to go. [Laughter.]

Senator Exon, I have not reviewed the authorization bill in detail, but I followed it more or less closely. And it has a lot of very positive things in it from the point of view of the structure of DOD, as well as the benefit of your in-house committee's consideration of the funding issues involved. I'm sure there is a major political issue involved with respect to the level of SDI funding, and I would rather imagine that that might have something to do with the decision whether or not to veto.

I lived through, as Under Secretary of the Navy, President Carter's veto of an authorization bill because it had an aircraft carrier in it. And although I had to salute and make the system work, I thought it created a good deal of disruption in our ability to effectively manage the Department of Defense that year. My strong hunch is that the same would be the case if it were vetoed this year.

Senator EXON. Thank you very much.

Mr. Packard, I listened with great interest to some of your personal experiences as a manager of one of our largest and most successful corporations. You made reference to the fact that one time a manager whom you appointed asked you to come down and tell all his subordinates that he was the manager. I was very much amused at your commonsense approach to that. As a former small businessman myself, I said amen when you said that.

Doesn't that experience that you just cited demonstrate better than anything else—you know, we can pass all kinds of laws, and we can make constructive suggestions as have been made here today and have been passed on the floor of the House and the Senate previously. The bottom line on proper procurement, free as it can be of improper activities, if any, comes down to the skills of hands-on management. You can't legislate morality in government and you don't try to legislate morality in the private sector.

Isn't this a management and management style as much as anything else given the fact that the far-flung bureaucracy and their ingrained position makes it much more difficult to manage than it does in private industry?

Mr. PACKARD. Well, I mentioned I think—in fact, I know—in my statement that you can't manage this defense acquisition business or other aspects of the Defense Department the same way you can manage business in the private sector. You have some entirely different conditions, and you have a political environment that you don't have in a private business.

There are, however, some fundamental aspects that apply to both. We have talked about those in the past, and I think we ought to continue to work on those.

One of the things, that troubles me particularly is this emphasis to approach this from what you might call a stick-only process. If you want to encourage better performance, there are two things you can do. You can use a carrot and encourage people to do a better job, or you can use a stick and beat them for not doing a better job. Well, it seems to me you have to do a little bit of both perhaps.

But one very interesting example came to my attention the other day that I think you might find amusing. It came from an experience in Old English law where they decided that pickpocketing was a very serious offense. In order to stop pocket-picking, they decided anyone caught picking pockets would be hung in the public.

So, they caught somebody, and they held a public hearing. There were a very large number of people that appeared at that hearing, and there were more pockets picked at that hearing than had been picked in the last 3 years. Now, I think that is the kind of a problem we have here.

Senator EXON. My time is up. I have just one last question, Mr. Chairman, if I might.

In the days of yesteryear, for good or for bad, we did have the Government involved in manufacturing. We had shipyards that would build ships and to an extent they were in direct competition with the so-called free enterprise system. We have all but done away with that now because we all believe in the free enterprise system and think that's the way to go.

Looking back to World War II when we did have Government-owned and operated shipyards in the manufacturing business, do you think that when we had that kind of a competition with the free enterprise system that it was a source of competition that probably provided some help in keeping costs down?

Mr. PACKARD. Well, I think there is an important issue here. I mentioned the Federal laboratories involved in defense as a specific example because I know something about those. And I think they did provide an element of competition with the private sector on some of these new development ideas that was very constructive. And I think that ought to be encouraged.

Now, I don't really know enough about the shipbuilding business to make any judgment. My inclinations would say that we don't really need to have nationalized shipyards. On the other hand, we are already to the place where you have only one organization able to perform some of these functions. To have that as an independent organization without any real competition poses a problem of control. And to put it back into the Government poses a problem. I think we just have to work with that as best we can.

We ought to try and get some incentives and get some better ways of really measuring what the performance is instead of all this paperwork that we use to evaluate it.

That issue of shipbuilding came up in connection with discussions in the commission in this revolving door issue. Secretary Lehman pointed out that he wanted to get some more experienced managers in charge of some of the Navy shipyards that are still operated by the Government, and he couldn't do that with the revolving door restrictions.

You get back to the issue that if you're going to use Government owned activities, you're going to have to find some way to attract and retain and motivate the kind of people you need to run those activities. So, these problems all tend to overlap.

Senator **Exon**. Mr. Packard and Mr. Woolsey, thank you very much. And continue, please, your great efforts of being of assistance to us who are very much involved in the process.

Thank you, Mr. Chairman.

Chairman **Nunn**. Thank you, Senator Exon.

Senator Quayle.

Senator **Quayle**. Thank you, Mr. Chairman. I want to again congratulate you for holding these hearings and taking us through this discussion. I think it is very important that we have a pretty good handle, particularly, with the two gentlemen that we have before us today.

I would like to ask a very simple question and one that you covered in your testimony, but I would like to narrow it down so I can have an understanding and perhaps a foundation of what you feel from your viewpoint—I would like for you to give me your three biggest disappointments on the implementation of the Packard Commission recommendations.

Let me start by saying that I feel that when we had these hearings—and at that time I was chairman of that Procurement Subcommittee—we were, as a matter of fact, almost to the point when we would get an amendment before our committee, we would want to call up and see what the Packard Commission people thought of this. A lot of recommendations in the Packard Commission said, "Well, there's not a lot that Congress can do. There's some. As a matter of fact, we don't want Congress to do too much."

From my viewpoint, I think Congress probably did about what you expected from a legislative viewpoint.

Could you give me, so I could have a better feel for it, the three biggest disappointments that you have had in seeing your recommendations being either benignly ignored or disregarded or not implemented?

Let me just say I have heard that there has been—at least the impression I have is that there is this concern that they haven't been implemented. I would like to just be able to put my finger on three of them that are very important to you that shows they just haven't followed what you had suggested because it had a very strong support here in the Congress and also I think—I know—on your commission.

Mr. **Packard**. Well, let me attempt to answer your question. I'm not sure that I can, off the top of my head, identify three, but I think there certainly are several.

One of my serious disappointments is the fact that the Defense Department did not pick up these recommendations with a great deal of enthusiasm when they were first presented and attempted to be implemented.

Now, this is not surprising for this reason, that the people who have been working there for 6 years together had been doing their best to accomplish things which they thought would improve the situation. It was not realistic to expect that they would be very receptive to recommendations that involved changing in a very substantial way what they had been doing in the past.

So, I think that that was, in a sense, a disappointment that they didn't pick these things up and push them a little more enthusiastically. On the other hand, it is understandable.

Senator **Quayle**. With what two or three of the recommendations would you have liked to have seen this enthusiasm to have them implemented that would have helped the procurement system?

Mr. **Packard**. Well, in many ways the most important one is this business of getting a better definition about the overall military strategy and tailoring our weapons acquisition program on the basis of what weapons are really necessary to support a national overall military strategy. Now, that involves some major changes. The structure was set up, but you had to get the services to agree that they would have less influence, and that was not anything you would expect to happen with any great urgency or any sense of expediency.

The second thing that I am very concerned about is that there tended to be still too much of a sense of using the stick rather then the carrot to encourage better performance. It seems to me you want to start with the proposition that almost all the people involved in this, whether in industry, in the Department or the Congress, are basically people of goodwill, and they are trying to do what they think is right. You're not starting out in dealing with a bunch of crooks by any means. The vast majority of the people are anxious to do a good job. It doesn't do the contractor any good to have these problems come up, and we ought to put more emphasis on a positive approach to these problems rather than a negative approach. That gets back to getting more incentives into the system.

Probably the other difficulty I think that has been very serious is the fact that despite this committee taking a very strong, positive role in moving ahead with the implementation of our recommendations, there are still quite a few people in the Congress that are using these things to attract attention to some of their personal projects and so forth. It would have been much more encouraging if you could have had a larger share of the Members of the Congress supportive of what this committee is trying to do.

Senator **Quayle**. You are talking about add-ons that Congress does or the micromanagement——

Mr. **Packard**. I'm talking about add-ons. I'm talking about getting up and proposing some new proposal that is going to settle things like an all-civilian procurement system or something else. You know what these things are I think, just as well as I do.

Senator **Quayle**. Mr. Chairman, can I go to a couple more questions? Let me go down these three things.

You are saying that the strategy doesn't necessarily fix, and that's the one that you focused on the most as far as a disappointment.

From your viewpoint as an overall strategy of the idea of the Competitive Strategy Task Force report—I don't know if you're familiar with that—which says that we ought to emphasize and look to the Soviets and our adversaries' weaknesses and exploit those and also at the same time exploit our strengths, would that be a good overall strategy that perhaps we ought to follow? What I'm trying to glean from you is where do we have this breakdown of not implementing an overall strategy with the procurement process.

Mr. **Woolsey**. Senator Quayle, is this the discriminate deterrence report by Iklé, and Wohlstetter?

Senator **Quayle**. No. This is the Competitive Strategies Task Force report. Discriminate deterrence is a separate one.

The Competitive Strategies Task Force report, which basically takes the proposition I just pronounced—there are some similarities because they do talk about a standoff capability. They talk about accuracy, but they talk about looking at the vulnerabilities of the Soviet Union as far as transportation and this, that we ought to be able to have systems that can go in to attack their vulnerabilities, but at the same time that we ought to look at our procurement system and perhaps enhance our capabilities like technology, like accuracy, like some cruise missiles, this type of thing. That's an overall strategy.

I think that is an overall strategy that has been accepted in OSD. I'm not so sure on record where the Joint Chiefs are and some of the services.

But is that the kind of disconnect—that you find that there is discussion perhaps of a strategy, but it's not accepted universally? Is this what we are talking about as far as your disappointment in strategy? Does either one want to comment on that? I'm trying to pin it down.

Mr. **Packard**. What you would like to do is to have a rational way at looking at all of these options that are available in terms of our military strategy and also in terms of the weapons that are involved. Right now you have these endeavors in the Congress, and I think some of them are talking about some very positive things.

But you have a whole bunch of random inputs to this business of trying to develop a better strategy. It seems to me that it would be much better if you could start with a system where you could take more time and consider these issues more carefully and not be just subject to all random inputs all the way across the board.

I'm not saying that all of these random inputes are wrong. Some of them I think are very good.

Maybe it is too much to expect. This is a difficult issue, and I think everybody realizes that. It would, I'm sure, be helpful if both the Department and other people in the administration and the Congress could have more time for some thoughtful discussions among themselves and consideration of these issues in trying to come up with a better definition of what we ought to be trying to do.

Senator **Quayle**. What about your carrot and stick approach? You say you would rather see the carrot rather than the stick incentives. Would you suggest, or did you suggest, some incentives for good ideas and incentives for R&D and some of the innovative concepts? Is this what you are talking about when you say the carrot and stick approach, that you prefer the carrot in some cases? Positive incentives?

Mr. **Packard**. I think the best example of this would be to put more emphasis on past performance.

Senator **Quayle**. On past performance?

Mr. **Packard**. It's not difficult to evaluate how well a contractor has performed on a specific contract. After it is done, you've got all the data there. You know whether they met the cost objectives. You know whether the equipment performed properly or whether it didn't. And you know a lot of other things about it. You have a basis of accurately evaluating how capable that organization is.

It seems to me that that's the kind of thing we ought to be looking at more carefully, and we ought to have some measurable evaluations of performance and put those at a much higher priority. Those include not only cost, but whether the weapons perform properly. That would get us a long way toward where we ought to be in this issue of determining the awarding of contracts.

Chairman **Nunn**. Senator Quayle, we have about 5 minutes left on a vote, and I'm not going to be able to return. So, if you could——

Senator **Quayle**. Why don't I close it out?

Chairman **Nunn**. Well, you could continue if you'd like and close it out.

Senator **Quayle**. Thank you, Mr. Chairman. I basically have exhausted my questions. I thank you.

Chairman **Nunn**. Well, I want to thank both of you, Dave Packard, Jim Woolsey, for being here. You've been a tremendous help as usual. We continue to rely on you, and we will have a continuing interest in this committee in not only the currect allegations, but also how we make our procurement system a better system for our own national security and for the men and women who rely on these weapons in the field. And so we thank both of you very much for your contribution.

Mr. **Packard**. Well, thank you very much for giving us the opportunity. I appreciate it.

[Whereupon, at 12:40 p.m., the committee was adjourned.]

THE DEFENSE ACQUISITION PROCESS

THURSDAY, AUGUST 4, 1988

U.S. Senate,
Committee on Armed Services,
Washington, DC.

The committee met, pursuant to notice, at 9:45 a.m., Senator Sam Nunn (chairman) presiding.

Present: Senators Nunn, Exon, Levin, Kennedy, Bingaman, Dixon, Warner, and Thurmond.

Staff present: Arnold L. Punaro, staff director; Romie L. Brownlee, deputy staff director for the minority; Jeffrey H. Smith, general counsel; Patrick A. Tucker, minority counsel; Jonathan L. Etherton, Sherri Wasserman Goodman, George K. Johnson, Jr., and James R. Locher III, professional staff members; Barbara L. Braucht, staff assistant.

Also present: Peter K. Levine, assistant to Senator Levin; Edward M. McGaffigan, Jr., assistant to Senator Bingaman; Charles C. Smith, assistant to Senator Dixon; Donald A. Mitchell, assistant to Senator Glenn; Terrence Lynch, assistant to Senator Shelby; and Anthony H. Cordesman, assistant to Senator McCain.

OPENING STATEMENT BY SENATOR SAM NUNN, CHAIRMAN

Chairman Nunn. We have had a vote on for the last 10 minutes and now we're in the final stages of the vote. After the vote, Senator Byrd has asked me to return because we have got to decide the sequence of bills coming up on the floor of the Senate. It is a question of whether to bring up the urgent supplemental or the Defense appropriation bill.

Therefore, I am going to have to leave and come back. Senator Exon, I am delighted you are here. I would like to get started with the hearing.

Senator Warner has a conflict this morning with the Environment and Public Works Committee and he will be unable to be present for the opening of the hearing, but hopes to come in later. We will have a number of members here. Senator Bingaman is now here.

So what I would like to do in the interest of time and to accommodate the witnesses—we are very delighted to have our expert panel here today—is for all of you to come up, and I will go back to the floor and leave Senator Exon in charge.

Go ahead and start the hearing, Senator Exon, and I will be back as soon as I can.

I did not make my opening statement.

Senator Exon. Do you want to do that?

Chairman Nunn. Why do we not just put the opening statement in the record. Let me just say by way of introduction of our witnesses, we have with us today three distinguished witnesses who have combined active involvement in Government service with serious and respected scholarship:

J. Ronald Fox, Professor of Business Administration at Harvard Business School, is a former Deputy Assistant Secretary of the Air Force and Assistant Secretary of the Army, with over 30 years of involvement in the defense acquisition process. Mr. Fox, we are glad to have you.

Mr. Lawrence Korb, who served as Assistant Secretary of Defense in the Reagan administration, is currently director of the Center for Public Policy at Brookings Institution, and he has been before this committee many times and contributed a great deal to our understanding of defense issues. I am glad to have you, Mr. Korb.

Richard Stubbing, who was responsible for the national security program for many years at the Office of Management and Budget, is now professor of public policy studies at Duke University and has a very distinguished record in the national security arena. We are glad to have you, Professor Stubbing.

Gentlemen, we would like to hear from all of you. Again, I will be back as soon as I can, and I would, Chairman Exon, ask that my entire statement be put in the record.

Senator Exon [presiding]. Without objection, that is so ordered.

[The prepared statement of Senator Nunn follows:]

Prepared Statement by Senator Sam Nunn, Chairman, Senate Armed Services Committee

This morning, the committee continues its hearings into the management issues raised by the recently exposed problems in the defense acquisition process.

Some observers have described the current scandal as a "procurement problem" caused by a few rotten apples. The witnesses we have heard from to date—Comptroller General Bowsher, Secretary Carlucci, David Packard, and Jim Woolsey—have consistently rejected such a narrow description. It is clear that the Packard Commission's 1986 description of the acquisition system as "fundamentally ill" remains valid today. As Mr. Packard told this committee last week, the acquisition system now operates in an environment "in which honest and efficient military acquisition is impossible to implement."

This committee has encouraged the administration to work with us in streamlining the acquisition system, but we have been disappointed at the level of cooperation we have received to date. In 1987, we sought to implement the Packard Commission's concept of a 2-year budget, but we were hampered by the President's submission of an unrealistic second year figure that was $20 billion over the Gramm-Rudman-Hollings requirements. Over the last 2 years, we have consistently urged the Department to submit legislative recommendations to remove impediments to innovation—yet all we received was a single proposal with several minor changes that even Under Secretary Costello dismissed as "pablum". The absence of quality efforts by the Department in these areas underscores the fact that complaints from the executive branch about congressional "micromanagement" are largely attempts to divert attention from DOD's own management failures—failures illustrated by David Packard's comment that the Department had "flunked out" on implementing the Commission's recommendations from streamlining the acquisition chain of command.

In the coming year, wise management of the limited resources available to defense will become increasingly important. In an environment dominated by tight budgets, we must ensure that the taxpayers—and our men and women in Uniform—receive the best return on their investment in our Nation's defense. Toward that end, today's hearing will focus on management—what deficiencies exist both in the broader management of the Nation's defense effort and in the current acquisition system, and what changes are needed.

We have with us today three distinguished witnesses, who have combined active involvement in government service with serious and respected scholarship. J. Ronald Fox, Professor of Business Administration at the Harvard Business School, is a former Deputy Assistant Secretary of the Air Force and Assistant Secretary of the Army, with over 30 years of involvement in the defense acquisition process. Lawrence J. Korb, who served as an Assistant Secretary of Defense, is currently Director of the Center for Public Policy at The Brookings Institution. Richard Stubbing, who was responsible for national security programs for many years at the Office of Management and Budget, is now Professor of Public Policy Studies at Duke University.

Senator EXON. Gentlemen, please proceed. I want to join in welcoming all of you here. Professor Stubbing, an old hand in Government and an old friend, Larry Korb, we are delighted to have you back again.

I think you know of the pressing issue that we are looking into and we are anxious for your expert opinion and advice as we pursue what to do and, I would emphasize, what not to do with regard to the problem that confronts us.

We will follow then in alphabetical order, as I understand it. So we will begin with you, Professor Fox.

STATEMENT OF J. RONALD FOX, PROFESSOR OF BUSINESS ADMINISTRATION, HARVARD BUSINESS SCHOOL

Mr. FOX. Thank you, Mr. Chairman. I appreciate the invitation to appear before this committee and I commend your efforts to deal with the underlying causes, rather than the symptoms, of defense acquisition problems facing the Department of Defense today.

I endorse the testimony of both Secretary Carlucci and David Packard before this committee, and I will offer several observations that I hope will contribute to their recommendations, and will explain why previous reform efforts have had limited success.

My complete statement has been distributed to you and other members of the committee, Mr. Chairman, and I would like to summarize that with considerably shorter remarks.

Senator EXON. Thank you, Mr. Fox. Without objection, we will accept the statements in full of yourself, Dr. Korb, and Professor Stubbing. All statements will be incorporated without objection in the record, and we appreciate your summarizing at this time. Then we will withhold questions from members of this committee until all of you have made your presentations.

Mr. FOX. Thank you, Mr. Chairman.

I have recently completed a 4-year study of the defense acquisition process and the barriers to improving that process in the past. The Harvard Business School has just published that study under the title "The Defense Management Challenge."

It is clear to me that problems in the management of the acquisition process span Democratic and Republican administrations. The problems are inherent in the system itself, a system that we have used to manage the process for nearly 30 years.

In my view, major reform is long overdue. Today, problems in the acquisition process take the form of consultants leaking proprietary Government information. Last month the problems were contractors making false charges to Government contracts.

Last year they were technical failures in defense programs. The year before that, it was unanticipated cost growth. The year before that they were high-priced spare parts.

The problem of leaking proprietary Government information is not new. I described that problem in my 1974 book, "Arming America." Unfortunately, most efforts to deal with these problems, though well-intentioned, have violated the same fundamental principle of business: When an organization undertakes a major program, it must assign persons experienced in industrial management, give them the authority needed to accomplish their jobs, compensate them well, and hold them accountable.

In my view, the Defense Department falls short on all those requirements. There's no doubt that program managers and their staffs are intelligent, hard-working, and dedicated persons. It is also clear that program managers, along with most other defense managers, genuinely want to acquire advanced weapon systems and other products that meet performance standards at reasonable costs.

Yet the Defense Department has attempted to manage multi-billion dollar programs by placing military officers and civil servants in impossible situations, asking them to control work performed by giant industrial firms, but failing to provide them with the tough negotiating skills, street smarts, and stable assignments required to deal with contractors on an equal footing.

In practice, too few Government managers know much about contractor financial incentives or about negotiating changes or controlling costs, schedules, and technical performance in large industrial firms.

As a result, Government managers rarely make the difficult decisions in defense acquisition required to create and reward lean industrial organizations, organizations that resist the expanding desires of functional managers in Government and functional managers in industry.

Today Government acquisition managers are often placed in a position akin to giving a new officer a few weeks of classroom instruction on flying, putting him in the cockpit of a jet fighter, and sending him on a combat mission. As ridiculous as this seems, it is equally ridiculous that most defense acquisition officers are given 90 days or less classroom instruction and then assigned to oversee defense procurement activities involving giant industrial contractors, complex technical specifications, contractor accounting systems, and millions of dollars.

Given limited authority and few tools to manage their programs, the officers often function as little more than briefing specialists and marketing managers, spending much of their time seeking additional funds and continued support for their programs.

This is hardly the prescription for high quality management, no matter how dedicated the personnel. As a crowning blow, military personnel who begin to develop experience in the acquisition process are forced out of the service at age 45 to 50, when most still have heavy financial commitments, including mortgages and children in schools.

DIFFERING PERCEPTIONS OF DEFENSE ACQUISITION

In reflecting on my interviews with people directly involved in defense acquisition, one outstanding impression is that Government and industry managers have widely differing perceptions on the current condition of the process.

Some describe it as poorly managed and plagued by serious problems. Others see it as well managed with few problems. The differing perceptions do not reflect the conventional dichotomies of military versus civilian or Government versus industry.

Rather, they reflect managers' differing views of the Government role in managing the defense acquisition process. It is these differing views (described below) that have served as one significant barrier to bringing about management improvement.

Many people in both Government and industry describe the job of Government program manager primarily as one of promoting a program, preparing progress reports and briefings, negotiating with officials at the Pentagon and various military commands, and resolving engineering conflicts between these organizations and contractors. They believe that the responsibility for cost control belongs solely to the contractor.

I call this the liaison manager view. It is based on the belief that the defense business is part of the free enterprise system and therefore regulated by competition in the marketplace.

Others describe the Government role as one of planning and making key decisions associated with rigorous oversight, negotiation and control of industrial firms that perform the development and production work. They believe the responsibility for cost control belongs to the Government program manager, the plant representative, and the contractor.

They also believe that significant cost reductions are often possible, depending upon Government managers' abilities to establish and implement challenging productivity and cost incentives throughout the life of a program.

I call this the active manager view. It is based on the belief that the competitive forces of the marketplace do not by themselves produce the desired cost, schedule, and technical performance on defense programs.

Those who hold the liaison view believe there is no need for Government program managers to have years of training and experience in industrial management and methods of cost control. If the program manager job is limited to promoting a program, preparing progress reports, and performing technical liaison, then experience as a pilot, tank commander, ship captain or engineer, and possibly 14 to 20 weeks at the Defense Systems Management College, may be sufficient.

But for those who hold the active manager view, as I do, military experience and 20 weeks of training, or even 2 or 3 years of training and experience, are insufficient for a manager of a large complex program.

Not surprisingly, those of the liaison view consider the Government acquisition job a reasonable alternate assignment or shore duty for combat arms officers until reassignment to their primary duties in operational units. Proponents of the active manager view, however, consider the defense acquisition process too complex, too costly, and too important to national security to serve as an alternate assignment.

People holding the liaison view often talk about cost control aspects of managing programs, but they fail to understand that the planning and control of large industrial development and production programs are achieved neither by proclamation nor by good intentions. They are achieved only by performing difficult analyses and tradeoffs, engaging in day to day negotiations, and making often difficult judgments. The skills needed for these tasks require years of intensive formal and on the job training and experience.

THE REVOLVING DOOR

Prudent military officers, encouraged by the military retirement system, as I mentioned earlier, often leave the service between ages 45 and 50 for positions in private industry, where their knowledge and skills can be developed and usefully employed.

Despite the Government's urgent need for well-qualified, knowledgeable acquisition managers, there are at present very few incentives for talented officers to remain in the military service beyond 20 to 25 years. The defense industry, on the other hand, provides compelling incentives: rewarding salaries and career status.

To address these incentives, I believe that the Government acquisition careers must be designed to attract officers and civilians to remain 5 to 10 years longer than at present and to develop the skills needed for this process.

One alternative for enhancing the acquisition career field would involve the establishment of a separate military service for acquisition managers, which has been done with considerable success in France. The service would need to include elite managers, military and civilian, dedicated to achieving the goals of the acquisition process.

Applicants would face an aggressive screening program to remove those who do not meet the high standards of the service. Advancement would be based strictly on management ability and performance.

Only senior acquisition officers, with no interference from combat arms officers, would control assignments and promotions. In addition, the corps would need a sufficient number of colonel or captain and general or admiral positions to reward officers for outstanding performance.

INCENTIVES

I would like to say a word or two about incentives. The Defense Department customarily manages weapons acquisition with a system of rewards and penalties that in my view are just the reverse of what they should be. Contractors are often rewarded for higher than planned program costs, with increased sales, contributions to overhead, and profits.

The system also encourages Government managers to place a far higher priority on gaining congressional approval to begin a new program or to obtain funding for an ongoing program than on controlling costs for existing programs.

The acquisition cost problems of the 1980s are not aberrations. They are the result of many Government and industry participants reacting in perfect accord with the distorted rewards and penalties inherent in the acquisition process.

New contract forms, better planning, control and reporting systems, or multi-year contracting are unlikely to be effective unless Government managers are skilled in the implementation and use of these techniques and are rewarded, along with the contractors, for their effective implementation.

Fundamental changes need to be made in the incentives applicable to Government program managers as well. They should be rewarded for effective use of formal and informal analysis and control techniques, for early identification of problems affecting costs, schedule, and technical performance, and for success in achieving program objectives and maintaining control of program costs.

At present, managers who handle crises effectively are given high performance ratings. Because preventive action requires day to day attention to management detail, inexperienced supervisors controlling the reward system are unlikely to appreciate the work of a good manager. As a result, there is often little motivation to exercise rigorous systematic control.

CONCLUSION

In conclusion, there is little likelihood that the costs of major defense programs will stabilize or decrease unless skilled Government managers at all levels have a strong commitment to the changes required to accomplish that objective. Minor adjustments or corrections or new techniques or new forms of contracts simply will not accomplish this vital job, nor will major reorganizations that seek to increase the decisionmaking authority of managers who lack the training and experience to manage the acquisition process efficiently.

The Defense Department needs to manage major programs the way they are managed in private industry. It needs well-trained, full-time, full-career industrial managers whose career development is treated at least as seriously as the career development of pilots or ship captains.

Failure to act now guarantees a continuation of the problems of cost growth.

That, Mr. Chairman, completes my prepared statement, and after my colleagues finish their statements I would be happy to address any questions that the committee may have.

[The prepared statement of Mr. Fox follows:]

TESTIMONY

BY

J. RONALD FOX

PROFESSOR OF BUSINESS ADMINISTRATION

HARVARD BUSINESS SCHOOL

Mr. Chairman. I appreciate the invitation to appear before this committee and I commend your efforts to deal with the underlying causes, rather than the symptoms, of defense acquisition problems facing the Department of Defense today. I endorse the testimony of both Secretary Carlucci and David Packard before this committee, and I will offer several observations that I hope will contribute to their recommendations and will explain why previous reform efforts have had limited success.

I have recently completed a four-year study of the defense acquisition process and the barriers to improving that process. The Harvard Business School just published that study under the title The Defense Management Challenge. It is clear to me that problems in the management of the acquisition process span Democratic and Republican administrations. The problems are inherent in the system we have used to manage the process for nearly thirty years. Major reform is long overdue.

Overview

Every few years, government commissions are appointed to study problems in defense procurement. Each time, the commissions recommend the same cures. Most people agree with the recommendations, but within a year or two, key defense managers change, the recommendations fade away, and a new set of problems emerge.

A close look at the current defense procurement scandal reveals that it is only the latest in a series of problems stemming from the federal government's long-standing shortcomings in industrial management.

Today these problems take the form of consultants leaking proprietary government information; last month they were contractors making false charges to government contracts; last year they were technical failures in defense programs; the year before that they were unanticipated cost growth; the year before that they were high-priced spare parts. (The problem of leaking proprietary government information is not new; I described it in my 1974 book Arming America)

Unfortunately, most efforts to deal with these problems, though well intentioned, have violated the same fundamental principle of business: When an organization undertakes a major program, it must assign persons experienced in industrial management, give them the authority needed to accomplish their jobs, compensate them well and hold them accountable. The Defense Department falls short on all of these requirements.

Defense Department officials oversee some of the largest industrial firms in the country, managed by well-trained, well-compensated, highly motivated managers who are very familiar with their companies' procedures for overhead allocations, profit calculations, cost estimating, performance measurement and return on investment.

Recently I talked with a group of industry managers new to the defense business and unaccustomed to the Defense Department methods. It was interesting to hear what surprised them about defense procurement.

As expected, they were unhappy with overly detailed government specifications, endless reporting forms, changes in funding, and the many audits. None of this is new. But the managers were stunned by the Defense Department's attempt to manage complex industrial programs with military officers, usually highly dedicated to their jobs, but who had little or no experience in industrial management. Indeed, at two major defense procurement offices with thousands of personnel, about half the military officers are lieutenants.

Some typical comments from the industry managers:

> "If we did this in the commercial world, we would be out of business in six months. . . ."
>
> "These government managers have little idea how our organizations work and what incentives apply to our managers."
>
> "The government invites contractors to play games by assigning inexperienced government managers to key positions, and then changing them every two or three years."

There is no doubt that program managers and their staffs are intelligent, hard-working, and dedicated. It is also clear that program managers, along with most other defense managers, genuinely want to acquire advanced weapon systems that meet performance standards at reasonable costs. Yet the Defense Department has attempted to manage multibillion-dollar programs by placing military officers and civil servants in impossible situations, asking them to control work performed by giant industrial firms, but failing to provide them with the tough negotiating skills, street smarts, and stable assignments required to deal with contractors on an equal footing. In practice, too few government managers know much about contractor financial incentives, or about negotiating changes, or controlling costs, schedules, and technical performance in large industrial firms. As a result, government managers rarely make the difficult decisions required to create and reward lean industrial organizations that resist the expanding desires of functional managers in government and industry.

Today, government procurement managers are often placed in a position akin to giving a new officer a few weeks of classroom instruction on flying, putting him in the cockpit of a jet fighter and sending him on a combat mission.

As ridiculous as this seems, it is equally ridiculous that most defense procurement officers are given 90 days or less classroom instruction, and then assigned to oversee defense procurement activities involving giant industrial contractors, complex technical specifications, contractor accounting systems, and millions of dollars.

Given little authority and few tools to manage their programs, the officers often function as little more than briefing specialists and marketing managers, spending much of their time seeking additional funds and continued support for their programs. That is hardly the prescription for high quality management, no matter how dedicated the personnel. As a crowning blow, military personnel are forced out of the service at age 45-50 when most still have heavy financial commitments, including mortgages and children in school.

The increasing complexity of defense procurement leads government and industry managers to hire thousands of consultants to assist in getting through the most complex maze in the field of industrial management. The consultants compete, each trying to outdo the other in gathering and distributing information. The process is now so complex that many consultants and contractors seek inside information as a near necessity, never viewing their actions as illegal--but as a legitimate way of conducting business.

The Relationship Between Government and Industry

The relationship between a government program office and its major contractor is necessarily a close one. Government and industry program managers must work together to solve complex technical problems, and, on finding solutions, they often need to initiate contract changes in the work being performed. In this environment, both government and industry must recognize that on development programs and most large production programs, a contract mechanism, by itself, is an ineffective substitute for rigorous day-to-day evaluations and negotiations. A government manager should not be simply a partner with private industry but an independent manager charged with supervising the use of public funds--that is, a wise buyer.

Defense contractors, though usually motivated by a commitment to a strong defense program as well as economic gain, have three important objectives: achieving the technical performance objectives of a program, meeting payrolls, and satisfying stockholders. Therefore, industry managers must continually strive to obtain additional contracts that will engage their R&D and production work force.

If the acquisition process is to run smoothly and efficiently, it should be structured so that contractors have a reasonable opportunity to earn returns comparable to commercial returns, without undermining government program objectives. When contractors perform well, government managers should be empowered to recognize that performance and to reward it with attractive profits and improved opportunities for future defense business. On the other hand, when contract terms are not complied with, government program managers and plant representatives must be sufficiently trained, experienced, and motivated to identify and report inadequate performance to higher echelons of the Defense

Department, and to search for corrective actions. Government officials at all levels of the Defense Department--and Congress--must be prepared to support this kind of responsible management.

Differing Perceptions of Defense Acquisition

In reflecting on my interviews with people directly involved in defense acquisition, one outstanding impression is that government and industry managers have widely differing perceptions of the current condition of the process. Some describe it as poorly managed and plagued by serious problems; others see it as well managed, with few problems. The differing perceptions do not reflect the conventional dichotomies of military versus civilian or government versus industry. Rather, they reflect managers' differing views of the government role in managing the defense acquisition process. It is these differing views that have served as a significant barrier to bringing about significant management improvement.

Many people--in both government and industry--describe the job of government program management primarily as one of promoting a program, preparing progress reports and briefings, negotiating with officials at the Pentagon and various military commands, and resolving engineering conflicts between these organizations and contractors. The responsibility for cost control belongs solely to the contractor. I call this the liaison manager view; it is based on the belief that the defense business is part of the free enterprise system and therefore regulated by competition in the marketplace.

Others describe the government role as one of planning and making key decisions associated with rigorous oversight of, negotiation with, and control of the industrial firms that perform the development and production work. The responsibility for cost control belongs to the government program manager, the

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plant representative, and the contractor. Significant cost reductions are often possible, depending on government managers' abilities to establish and implement challenging productivity and cost incentives, formal and informal, throughout the life of a program. I call this the active manager view; it is based on the belief that the competitive forces of the marketplace do not, by themselves, produce the desired cost, schedule, and technical performance on defense programs.

Those who hold the liaison view believe there is no need for government program managers to have years of training and experience in industrial management and methods of cost control. If the program manager job is limited to promoting the program, preparing progress reports, and performing technical liaison, then experience as a pilot, tank commander, ship captain, or engineer, and possibly fourteen to twenty weeks at the Defense Systems Management College may be sufficient. But for those who hold the active manager view, military experience and twenty weeks of training--or even two or three years of training and experience--are insufficient for a manager of a large, complex program.

Not surprisingly, those of the liaison view consider the government acquisition job a reasonable alternate assignment, or "shore duty," for combat arms officers until reassignment to their primary duties in operational units. Proponents of the active manager view, however, consider the defense acquisition process as too complex, too costly, and too important to national security to serve as an alternate assignment. I strongly agree with the active manager view.

People holding the liaison view often talk about the cost-control aspects of managing programs, but fail to understand that the planning and control of large industrial development and production programs are achieved neither by proclamation nor by good intentions. They are achieved only by performing difficult analyses, and trade-offs, engaging in day-to-day negotiations, and making often-difficult judgments. The skills needed for these tasks require years of intensive formal and on-the-job training and experience.

Reexamining the Program Manager Concept

The program manager concept works well in industry. But a fundamental flaw exists in the way the Defense Department has implemented the concept of a government program manager controlling a giant industrial firm. Consider the unique characteristics of industry program managers, who usually report to the company president.

1. They have genuine decision-making authority regarding personnel assignment, promotions, technical matters, and budgets.

2. They have years of training and experience in the operations of the industry relevant to the program (e.g., development and production of missiles, aircraft, tanks, ships. guidance systems).

3. They understand the roles performed and the tactics employed within government, within industry, and between government and industry.

By contrast, DOD acquisition managers often lack the training, experience, and stature of their private-sector counterparts. They also encounter another serious obstacle to performing their jobs. Namely, they are required to respond to (indeed, often placate) many individuals capable of influencing their career: people in the buying command, the using command, the service headquarters staff, the service secretariat, OSD, and the Congress. Within these groups there are diverse elements: some who support the program, some who oppose it, and some who are undecided. The people representing one or more of these groups change every few months, as assignments change. These people continually ask questions and have voracious appetites for data from program managers: How much will it cost to reduce the aircraft by 200 pounds? What is the consequence of reducing the budget by $300 million? How much can we save by reducing the production rate by 50 percent? How much will the reduced rate increase unit costs? What will be the impact of replacing the radar? What caused the delay? What will it take to regain the lost schedule? How much can we save by competing the next production contract?

If DOD is to manage the acquisition process more effectively and efficiently, it is time to change the current method of manning and operating program offices. The current job descriptions portray program managers as supermen who

- cut through the red tape laid by several hundred "interested" government managers;
- always obtain budget approvals from the service headquarters, OSD, and the Congress;
- work as partners with industry in solving technical problems;
- obtain reliable measurement data from which to determine independently a program's schedule, cost, and technical performance status of a program; and
- provide incentives for industry to perform expeditiously at the lowest reasonable cost.

Program managers are expected to accomplish all this with an underpaid and inexperienced staff operating within a procurement system that rewards higher costs and penalizes lower costs.

After nearly thirty years, we know that an Army or Air Force colonel or Navy captain (0-6) can rarely orchestrate and control a giant contractor and a series of government organizations headed by individuals significantly his senior. If DOD is to perform the role of the wise buyer, a two-star or three-star commodity commander (e.g., NAVAIR, MICOM, ASD, ESD) must play the role of the active program manager; lower-ranking senior military officers and civilians, well trained and experienced in the acquisition process, will be needed to gather and analyze data and implement program decisions. The commodity commanders must be highly skilled in the acquisition process and business management, and committed to effective and efficient performance; there is too much at stake for on-the-job training in these positions.

The Need for Acquisition Careers

My research leads me to conclude that people assigned to key acquisition positions--at every level in the Defense Department, from program managers to appointees in the Office of the Secretary of Defense--are often seriously unprepared for their jobs. One of the conclusions from studying the acquisition process is that managing it requires specific knowledge and skills well beyond those of many recent Assistant Secretaries, senior military officers, program managers, and congressional staff members.

There has long been an implicit assumption within the Defense Department that people with little or no advanced training and experience in the management of large industrial programs could function effectively at any management level.

This assumption has been a key factor leading to the disappointing results of virtually every improvement program in the past twenty-seven years. If the complex defense acquisition process is to be managed more effectively and efficiently, the Defense Department must develop better trained and more experienced acquisition managers and support staffs to manage the complex, continuing negotiations between one part of government and another and between government and large industrial firms. There is no realistic alternative to providing clear acquisition career paths for these people--both military and civilian--with genuine promotion opportunities comparable to those provided in operational career fields. Short of these steps, the department can expect yet another decade or more of studies and recommendations for improvements, with little accomplished in the way of lasting change.

It seems only reasonable that the heads of the Army, Navy, and Air Force acquisition organizations should be among the most qualified acquisition managers available, based on many years of training and practical experience. When selected for these positions, they should have sole responsibility for materiel acquisition and personnel recruitment, selection, and assignments. To separate these responsibilities is to invite the problems of the past three decades.

Program managers' careers should follow a path similar to those of Army brigade commanders, Air Force wing commanders, and Navy wing and ship commanders. Not only do military operations jobs have well defined career paths that include training and practical experience, but they are centrally managed by formal career development systems to ensure that all supervisors are fully aware of the career requirements. As late as 1987, there was insufficient attention to career development for most military officers and civilians assigned to defense acquisition. The Air Force has developed a promising acquisition career program (for non-rated officers) that stands as a good example of what needs to be done. The Navy uses a centralized approach through their Weapon Systems Acquisition Management (WSAM) and Material Professional (MP) programs, but they fall far short of the goal, from a career development perspective, for unrestricted line officers. The new (1983) Army Materiel Acquisition Management (MAM) program lacks central control and authority and provides too little training and practical experience too late in Army careers.

Although the twenty-week Defense Systems Management College course is an important first step in training program managers and their staffs, much more needs to be done to train them to an acceptable level of performance. The current policy of limiting this training to 138 days, because of regulations concerning moving-expense reimbursement, must be changed. Compared with the multibillion dollars involved in the acquisition process and the opportunities for savings, moving expenses are trivial.

Future program managers should be required to complete a minimum of one full year of formal training in which they study hundreds of examples of the dilemmas both they and contracting officers will encounter. They should analyze these dilemmas and discuss the strengths and weaknesses of alternatives available for dealing with them. Instructors skilled in conducting the practical training--those comfortable with interactive sessions requiring current practical knowledge of the field--will require attractive compensation. The training program should develop the "wise buyer" skills needed to resolve the multitude of complex day-to-day problems in major R&D and production programs. The emphasis should be on making analyses and decisions, using simulation exercises, case studies, role playing, and other techniques. An internship in a program management office would ideally precede and follow the one-year practical training program; carefully chosen program managers would serve as supervisors.

The Revolving Door

Prudent military officers, encouraged by the military retirement system, often leave the service between ages forty-five and fifty for positions in private industry, where their knowledge and skills can be usefully employed. Despite the government's urgent need for well-qualified, knowledgeable acquisition managers, there are at present very few incentives for talented officers to remain in the military service beyond twenty to twenty-five years. The defense industry, on the other hand, provides compelling incentives: rewarding salaries and career status.

However, the need to later obtain a job in industry can easily have a subtle effect on a person's performance while in government service. Industry positions are offered, understandably, to those who have demonstrated an appreciation of the particular problems and commitments of industry. Unfortunately, government and industry goals regarding costs are rarely identical. To address these differences, acquisition careers must be designed to attract officers to remain five to ten years longer than at present.

If, as has been the case for nearly three decades, the military promotion system will not respond to repeated attempts to provide attractive promotion opportunities to flag rank, then the Defense Department should provide other incentives, such as additional pay. If an extra $15,000 per year were paid to selected military officers (at the rank of O-6 and above) and career regulations permitted them to remain in the acquisition field, incentives to retire and join the defense industry would be greatly minimized. The extra cost would be negligible compared with the benefit of retaining experienced senior managers.

If an incentive pay plan were adopted, there would need to be a group of senior acquisition officials to determine the eligibility of those choosing an acquisition career. Otherwise, program management could become a haven for officers not qualified to enter the competitive world of private industry. Selection for these financial incentives could offset, at least partially, the lack of promotion opportunities in the acquisition field.

Such a proposal is not without precedent. Military officers on flight status and submarine duty as well as medical and dental officers and other special-skilled officers currently receive incentive pay. Indeed, Sweden's government acquisition agency addresses the problem of attracting and retaining senior people--military and civilian--by a special law that allows an added salary increase for crucial acquisition positions. Thus, a Swedish colonel serving as a program manager can receive a significantly higher salary than other colonels and even the director general of the agency. This incentive provides prestige and draws highly qualified, experienced people to senior acquisition positions.

A second alternative for enhancing the acquisition career field would involve the establishment of a separate military service for acquisition managers, which has been done with considerable success in France. The service would need to include elite managers dedicated to and capable of achieving the goals of the acquisition process. Applicants would face an aggressive screening program to remove those who do not meet the high standards of the service. Advancement would be based strictly on management ability and performance. Only senior acquisition officers, with no interference from combat arms officers, would control assignments and promotions. In addition, the corps would need a sufficient number of colonel or captain and general or admiral positions to reward officers for outstanding performance.

If a more attractive government career in acquisition management is made available, it would then be possible to minimize the conflicts associated with widespread military retirements to industry, while preserving the rights of individuals to full-length careers. The basic goal of any legislative remedy must be restoring the integrity of our military procurement system.

The current military promotions and retirement system, which forces out most officers in their 40's, is based on maintaining youthful forces for the demands of combat. Providing for longer careers in procurement would slow the "revolving door" between the military and its contractors. If outstanding procurement officers were encouraged to work for another five to 10 years, it would reduce the need for consultants and reduce the incentive to join the more lucrative defense industry.

Incentives

The Defense Department customarily manages weapons acquisition with a system of rewards and penalties that are just the reverse of what they should be. Contractors are often rewarded for higher than planned program costs with increased sales, contributions to overhead, and profits. The system also encourages government managers to place a far higher priority on gaining congressional approval to begin a new weapon program or obtain additional funding for an ongoing program than on controlling costs for existing programs. The acquisition cost problems of the 1980s are not aberrations; they are the result of many government and industry participants reacting in perfect accord with the distorted rewards and penalties inherent in the acquisition process.

New contract forms, better planning, control and reporting systems, improved cost estimating systems, and change control systems are unlikely to be effective unless government managers are skilled in the implementation and use of these techniques and are rewarded, along with the contractors, for their effective implementation.

Encouragement is not enough; improvements in management require significant changes in the system of rewards and penalties. Reluctance to establish more appropriate incentives has been a serious deficiency in most DOD improvement programs during the past three decades. As defense analyst Richard Stubbing has observed: Contractors should be rewarded with higher profits for complying with schedules, satisfying promised performance standards, and delivering goods and services at or below contracted cost. Conversely, penalties, in the form of reduced profits, should be imposed for late delivery, substandard work, and cost overruns. Prospects for obtaining future contracts should be closely linked to performance on existing contracts.

Equally fundamental changes should be made in the incentives applicable to government program managers. Government program managers should be rewarded for effective use of formal and informal analysis and control techniques; early identification of problems affecting cost, schedule, and technical performance; and success in achieving program objectives and maintaining control of program costs. At present, managers who handle crises effectively are given high performance ratings. Often, however, timely preventive action could have corrected problems before the crisis. Because preventive action requires day-to-day attention to management detail, inexperienced supervisors controlling rewards are unlikely to appreciate the work of a good manager. As a result, there is often little motivation to exercise rigorous, systematic control.

One effective way of measuring management performance is by evaluating a manager's use of contingency funds. Such funds, which could be held in reserve by senior defense officials, would be available only on request. Program managers finding it necessary to apply for contingency funding would be rated negatively, unless able to prove just cause. (Just cause could include the decision to expand an R&D program to reduce production or support costs.) Those able to remain within budget would be rated positively.

Many in government and industry want to improve the acquisition process. But it is unrealistic to expect any lasting improvement if an appropriate system of incentives and disincentives is not established and enforced. For example:

-- Unless changes are made in the current contractor source selection process, which makes optimistically low cost estimates a significant advantage in competing for a contract, it is useless to discuss realistic contractor proposals. The source selection process must give far more weight to realistic cost estimates and the contractor's record of past performance.

-- Unless changes are made in the current profit system that demands higher costs as a prerequisite for higher profits, it is futile to expect lower costs. Because profits are largely cost based, there is little economic motivation for contractors to reduce direct or indirect costs. The profit system needs a major overhaul to relate profit more to contract performance than to the level of costs.

-- Unless changes are made in the current military personnel system that makes short-term assignments necessary for military officers to acquire the number and variety of assignments required for promotion, any significant reduction in personnel turnover in defense program offices is unlikely.

-- Unless changes are made in the current OSD and congressional practice of routinely accepting program stretch-outs as a tactic for funding new programs, it is unrealistic to advocate economical production rates.

-- Unless changes are made in the current DOD practice of waiving training requirements and offering only short training courses, which limit coverage to introductory rather than in-depth treatment of important subjects, it is unrealistic to expect improved training for acquisition managers.

-- Unless changes are made in military careers that currently provide few opportunities beyond age forty-five or fifty, it is unrealistic to expect military officers not to seek a second career in the defense industry. In addressing this problem, DOD needs to listen to lieutenant colonels and colonels and Navy commanders and captains to learn their views on the advantages and disadvantages of the acquisition career field.

-- Without genuine promotion opportunities for individuals who make the difficult decisions associated with successful negotiating and wise buying, it is unrealistic to expect to retain in government service experienced government program managers able to do much more than promote their programs, prepare progress reports, and conduct briefings.

Incentives and disincentives are clearly key factors in improved defense acquisition management. In the commercial sector, rewards accrue to those who manage effectively and efficiently the resources assigned to them and who demonstrate high profitability. In the government sector, because there are no profit and loss statements by which to measure efficiency, the benefits from improved management are difficult to measure. Unfortunately, efforts to improve efficiency often generate political opposition from those who benefit from the existing inefficient practices.

The Need for Extended Follow-up Action

There will be no lasting improvements in the defense acquisition process until military commanders, beginning with the chiefs of staff, are convinced that the high cost of weapons and equipment is a serious problem that must be solved. The mandate to change must come from the top; only then will there be changes in the daily activities of defense managers.

Gilbert W. Fitzhugh, Chairman of the President's 1970 Blue Ribbon Defense Panel, noted that when studies are completed and committee members depart, those who remain to assess and implement recommendations are those whose "toes have been stepped on" in the findings. There is, not unexpectedly, a noticeable lack of enthusiastic support. Those responsible for implementation need an advocate remaining on the scene to lend support to the findings with understanding and conviction. The report of the 1986 Packard Commission has encountered the same problem. In early 1987, a Pentagon official told us:

> The official word is, the Packard Commission recommendations have already been implemented. Have they been completed? No. It will take as long as the next reorganization to implement them.

It is clear that the military and civilian leadership will need to be unambiguous in declaring the steps to be taken to improve management of the acquisition process and persistent in the follow-up to ensure that the changes take place.

Prospective

Because of the immense size of the defense acquisition budget, any changes or system improvements in the process have the potential for achieving significant savings. Estimates range from $10 billion to $40 billion per year, without reducing the output of weapons and equipment. In light of the opportunities to be gained from stabilizing funding, reducing contract changes, and adjusting the cost incentives for government and industry managers, I believe potential savings are closer to the upper end of that range--$40 billion per year.

There is little likelihood that the costs of major programs will stabilize or decrease unless skilled government managers, at all levels, have a strong commitment to the changes required to accomplish that objective. Minor adjustments or corrections to the present acquisition process simply will not accomplish this vital job, nor will major reorganizations that seek to increase the decision-making authority of managers who lack the training and experience to manage the acquisition process efficiently.

In summary, the Defense Department needs to manage major programs the way they are managed in private industry. It needs well-trained, full-time industrial managers, whose career development is treated at least as seriously as the career development of pilots or ship captains. Failure to act now guarantees a continuation of the problems of cost growth, reduced defense capability, and increased risks of major financial crisis for the country.

That, Mr. Chairman completes my prepared statement. I would be happy to address any questions that the Committee may have at this time.

Senator EXON. Professor Fox, thank you very much.

We will now go to Dr. Korb. Dr. Korb, welcome back again.

STATEMENT OF DR. LAWRENCE J. KORB, DIRECTOR, CENTER FOR PUBLIC POLICY EDUCATION, THE BROOKINGS INSTITUTION

Dr. KORB. Thank you, Senator.

It is nice to be here, but I wish it were under different circumstances. It seems like we can never go beyond scandals and horror stories to the real business of the Congress and the Department of Defense, which is to provide a strong, effective national security for the country.

I would like to do two things today. I would like to touch on the current so-called scandal, primarily from the point of view of accountability. I know you have had lots of people come up here and say, "Well, we need to look at the lessons." Certainly that is true, and I will focus on the lessons for the overall management of the Department in the second part of my testimony.

I think it is also important that we lay some blame for this current situation. As we look at the current scandal, it is important to keep in mind that you cannot design a foolproof system. If you had a foolproof, error-free system, you probably would not be producing very much of anything.

Also, the greed in the Department of Defense is not new, especially in times of large defense buildup. If the allegations that have been made so far are correct, we have never seen systematic greed at so high a level. Previously, when people at this particular level were alleged to have been involved in a procurement scandal, it has usually been to prevent information about development problems or cost overruns from becoming public.

Yet, if control from the top is relaxed, checks and balances within the system are removed, warning signs are ignored, and you provide a climate where scandals like the current one can flourish.

Now, you have heard people come up here before you, Mr. Packard, and talk about the fact that the Secretary of Defense cannot manage the procurement process or make contracting decisions, and I think everybody would agree with that.

However, a Secretary of Defense simply cannot undertake a rapid buildup and relax controls if he or she knows the history of the Department, namely that scandals usually erupt when there is lots of money in the system. A Secretary of Defense cannot simply remove himself from the process of appointing high level people in the Department of Defense.

A Secretary of Defense cannot allow a service like the Air Force to be the program manager for the B-1 and then expect that program to come out the way that it should. We cannot have a Secretary of Defense who sits back and does not intervene when one service, in this case the Navy, sets down its own procurement rules which were different from the rest of the Department and then be surprised when chaos is created in the defense industry.

You cannot have a situation where the Secretary and his staff do a profit study, the so-called DFARE study, then allow one service, in this case the Navy, to do its own which contradicts the one which the Secretary of Defense has done.

You cannot have a situation where the Secretary of Defense removes himself completely from the procurement process to the extent he will not meet with contractors who have problems in trying to figure out what, in fact, is Department policy. You cannot have a situation in which one service, in this case the Navy, was allowed to disestablish its major buying command without any analysis of consequences.

Similarly, you cannot have a situation in which one service Secretary, in this case the Secretary of the Navy, runs roughshod over all opposition, internal and external; politicizes the promotion, evaluation, and procurement process; makes arbitrary decisions about the procurement process which allows political appointees to override career people; and make outlandish claims that cannot be accepted at face value, for example—the price of the F/A-18.

Similarly, industry which has, and I think quite correctly, to police itself—and I accept the recommendation of the Packard Commission that it do so because you simply cannot have one auditor or one inspector per worker—but if industry is to do that, then it simply cannot go out and hire consultants who are known to have, at best, unsavory reputations in the hope that they can help them win contracts.

Having said that, what are the lessons for the management of the Department of Defense? I think this situation and certainly other situations in the last couple of years have shown us that there is no substitute for an acting Secretary of Defense with a strong staff and with the power to hire and fire people throughout the Department of Defense.

A Secretary of Defense cannot merely set fiscal goals or work on selected issues. As we look at the Department, the procurement process is not the only process in disarray. I think one could talk also about the budget process.

If we look at the Department as we come to the next administration, I think we have to look at not just the Secretary of Defense but the management team in the Department of Defense.

I think it is very important that we have a coordinated and complementary management team at the Department of Defense. If the Secretary of Defense is to handle issues outside the Department—dealing with the Congress, our allies, the National Security Council and the media—then we need a strong Deputy Secretary of Defense who will manage the budget process and the day-to-day operations of the Department of Defense.

We need an Under Secretary of Defense for Acquisition with a very strong acquisition background to handle that particular process, and then, although it is not the subject of this hearing, we need a strong Under Secretary for Policy, who will help the Department develop the strategy that will guide both the procurement and the budget systems.

And we must ensure that the skills of these individuals complement one another. We need somebody from industry, we need people with a strong political background, we need people who are acquainted with defense industries.

Similarly, in appointing service Secretaries I think it has to be clear to the Congress and the American people in the industry that the service Secretaries are "vice presidents" of the Department of

Defense and not independent agents. "Vice presidents" who are there to ensure that the services carry out the wishes of the Secretary of Defense and the President and not establish their own priorities.

In this I think it is important that the Secretary of Defense be the one who has the power to hire and fire service Secretaries. We also have to ensure that all people appointed to high positions of responsibility in the Department of Defense have a dedication to public service in the public interest, not to their own goals.

We need to increase the professionalism, the pay and prestige of procurement and acquisition personnel, and I support the efforts of Senator Bingaman to move in this particular direction.

If industry wants to regulate themselves, and I think they have to be responsible not just for their own employees, they have to be held accountable for people who they hire as consultants.

And finally, as Senator Exon talked about, we have to urge what not to do. I do not think we need to tighten the revolving door anymore. I think the law that went into effect in mid-April of 1987 certainly does what needs to be done.

But I think we have to be careful, because we have to ensure that in the next administration we are able to get good people in, people with experience in the acquisition process. If we tighten the revolving door any more it will not be a question of what they do when they leave—we will not get the private people in.

Thank you very much, Senator.

Senator EXON. Thank you, Dr. Korb. We are now pleased to recognize Professor Stubbing.

STATEMENT OF RICHARD A. STUBBING, PROFESSOR OF PUBLIC POLICY ANALYSIS, DUKE UNIVERSITY

Mr. STUBBING. Mr. Chairman, I would like to address two things today—one, the underlying problems that we face in defense procurement purchasing, and an agenda I would like to suggest for the incoming President to clean up the situation.

The problems in defense today permeate the entire defense culture. Mr. Robert Costello, the acquisition executive, suggested up to $50 billion of the $170 billion we spend each year for purchases in the Department of Defense are lost due to inefficiencies—$50 billion.

What does that mean? Fifty billion dollars can be equated to one-third of the Federal deficit. It is five times the total NASA budget, or it is three times the total budget for the Department of Education. That is a lot of money.

The first point I would make is that these are not new problems we are looking at today. They started back in the 1950s, when we made a major change of policy, for the first time in our Nation's history, to carry a large peacetime military force and a defense industry structure to go along with it.

When we set up, or allowed to continue after the Korean war, a defense industry, we allowed it to be insulated from the normal laws of the marketplace. So the problems had incubation in the 1950s, and they have grown.

Two things happened in recent years to make the problems as serious as they are today.

One is we gave the Defense Department far too much money too fast in the early 1980's. And, second, there was a managerial vacuum at the top in the Pentagon. The result, as I see it, is the defense world right now is out of control and definitely needs to be reined in.

What are these underlying problems? Let me identify several of them. The first is one I mentioned a moment ago. Defense contractors operate in a protective cocoon, not part of the free marketplace.

Let me give you some rules that operate in defense contracting, as I see it. No outsider—I am talking now about major contractors—no outsiders need apply. The major contractors we have today in defense are the same contractors we had in 1960. And no others have arrived.

The contracts tend to be spread around among contractors. There is a lot of political interference in the awarding of contracts. I cite one—the Boeing Corporation, just to pick a company. In my 20 years in Government I have just marveled at what happened to them.

This is a company that has a fairly successful commercial business, unlike many of the major aerospace contractors, and on six distinct occasions that I can remember while I was in Government, Boeing lost every single major contract it tried for.

In each case, they were a finalist in the competition. In several of the cases, they were the choice of the service. In every case they lost to a company who either was in deep financial trouble or whose business base was fast eroding and they needed business bad—in every single case, an interesting story.

Another aspect of the current contracting situation is there are minimum penalties for poor performance. When a contractor does not perform, the penalties are not there and in fact, at times they get rewarded.

Financial setting is also highly attractive in defense work. There is low financial risk. We pay tremendous progress payments which carry the loans or borrowing that most corporations would have to go out and do.

The pay is, by all studies that I have read of contractor personnel, higher than their peers in other durable good industries and defense contractor profits, as the studies show, range in terms of return on assets two to three times that of other durable good industries in recent years. So it is a very attractive financial setting for the folks that are in it.

And then we have this problem of continuing production lines too long. We are doing that today on a number of lines, but it is a continuing problem and really, in terms of cost to the Government, every penny we spend on these extended production lines is an inefficiency to the U.S. Government, to the taxpayer.

Those are some of the problems that I see in the industry. The second broad problem is that we have, as I see it, too many regulations, too many laws, too many consultants, too many lawyers, too many powerful interests opposed to the changes that need to be made.

With the help of the Senate staff here and the Department of the Navy, I would like to present a visual display of one of the big problems in the regulations that have crept in over the last 30 years in the Department of Defense. And if I may, I will show you.

These are the operating instructions that the people in the U.S. Navy have to operate on to make the contracts work and that they have to enforce. Now, I would suggest, Mr. Chairman, that this is an impossible task.

No one could possibly know what is in these 30,000 pages of regulations. We have allowed ourselves to be over taken by bureaucratese and protecting one's interest, and we have created a monster that needs to be fixed.

Senator **Exon**. I would suggest, Professor Stubbing, if you have any more exhibits, that we get a forklift.

Mr. **Stubbing**. You have seen my exhibits.

Senator **Kennedy**. Are those regulations for different systems or exactly what are those?

Mr. **Stubbing**. These are the regulations for contracting, Senator, for the Department of the Navy.

Senator **Kennedy**. For any contracting?

Mr. **Stubbing**. You have to then reach in and find out which ones apply to them, but there are rules and regs in each of these that the people have to be conversant with.

Senator **Exon**. But, Professor Stubbing, for example if you were going to buy fatigue uniforms, all of that would not apply. There would be a section for clothing, I suppose?

Mr. **Stubbing**. You have to know where to go to do that part of it, yes. But lots of it overlaps from one book to another and it is a particularly complicated system.

Senator **Exon**. It is not necessary for you to move that. We have no liability insurance.

Mr. **Stubbing**. But I did want to dramatize that this is out of control and we must do something about that.

A third problem area that I would identify is there is simply a lack of hands-on managerial attention to the problems that we see and to the corrective actions that are required. Finger pointing is not in, but I must say that the lead in the corrective action, the problems start and need to be corrected starting at the Pentagon. You in the Congress have contributed to them also, but the primary fix, I think, has to come out of the Pentagon.

What are some of the problems in managerial style that I would point to? In the broadest sense, one would be the budget process. We spend far too much time, in my judgment—I am a budgeteer—on budget preparation and the selling of the budget, and just a hopelessly inadequate time on the execution of the budget.

When I worked in industry many years ago, at Eastman Kodak, it took them 3 months from the time we started the budget process to get approval of the Board of Directors.

The Department of Defense annual budget takes 21 months. It starts 21 months prior to the start of the fiscal year—21 months for the annual budget. It is madness to me. We have really let it get out of control.

We devote inadequate attention in the weapons world to the critical first steps of determining the threat and the requirement. We do not spend adequate time on these and we pay a big price for that failure.

How we acquire the weapons and then, as both Larry and Ron indicated, the incentives that we provide are often perverse to people who work for government and who work for the contractors.

Now let me try and summarize these things in a single chart. This is a little easier. What I would like to do with the chart is to use the chart to explain to you the theory and the practice of major weapons acquisition.

The left column has six steps, which is the theory of how we buy weapon systems. We start with a defined threat—sensible; we should do it.

The next step is to define our requirement to meet that threat. Sensible. Next we get the contractor. We go out and have a competition and find a contractor. Then we develop and test the weapon. Then we produce the weapon, and finally we support it in its operational life. That is the theory of how we buy weapon systems.

The reality is quite different from the theory, and I would like to tell you about four systems we have done in past years that I am familiar with. I picked one from each service; they are certainly representative of how it works.

The threat was overstated in connection with the M-1 tank. In this case, we projected a Russian tank that was not real but it helped to sell the program at the beginning. And then we had a goldplated system. Because we saw a Russian threat that was not there, we pushed the technology to make our tank more advanced than it had to be against the threat that was more realistic.

In the case of the M-1, we also had a problem of political interference. In 1976 the contractor picked by the Department of the Army to win the award was ruled out by intervention at the last moment by the Secretary of Defense, who decided to change the requirement for the tank at the 11th hour and 59th minute of the competition. The change in requirement that he pushed allowed the losing contractor to become the winning contractor. Development and testing were inadequate on the M-1.

We produced it too soon because we did not do enough testing and this tank has been very expensive to maintain.

The F/A-18 is a Navy aircraft. In this one there are a couple of "OKs" on here. The threat estimate was reasonable.

Surprisingly, the top Navy brass were opposed to the weapon, but they got a lot of political help to change their mind from their civilian leaders in DOD and from people on the Hill, and they decided to buy what is, in effect, a dual purpose airplane which is not the normal Navy approach.

In fact, the Navy seldom buys dual purpose airplanes, and this one is a fighter to shoot down other airplanes and it is an attack airplane to drop ordnance as required. It is hard to do both, and we found out it was hard to do both. As a fighter, the F-18 turned out to be okay.

But in the critical power projection mission of the carrier, to which this airplane is assigned, this was not a good weapon. It did not do the job. I will just read a quote from the 1982 Navy operational test report—I still to this day marvel that we buy these kinds of weapons—describing the A-18, which is the attack aircraft.

The ability to deliver ordnance is the carrier's critical mission, the most important mission the carrier has is that. Here is the Navy OPTEV for evaluation of the A-18, "Our current ability to engage the Soviet fleet will markedly diminish and the vulnerability of our carrier forces will be of major concern." We have spent $30 billion on this program, and it says we have less capability than we had before. It is madness.

The F-15 is the famous story of the MIG25 Foxbat in which the intelligence people in the Air Force greatly overstated the capabilities of the MIG25, which we then later found out, when a Soviet defector landed in Japan, that it was a bucket of bolts.

But nevertheless, it helped to sell the F-15, which then became a very advanced technology airplane. We ran into lots of problems with this aircraft in cost and in performance.

All three of these programs, by the way, went the paper competition route which is not unlike what I just showed you for the regulations—paper on top of paper, promising everything but, unfortunately, in every one of these cases, unable to deliver.

And the rest of the program was the same—inadequate, too soon, high cost; three big programs, one for each service, all with tremendous problems. As a contrast, I show one success story. There were not many in my years in Government. One was the F-16.

I believe there are some lessons to be learned from the F-16. They did not have problems in terms of an overstated threat. They went out with broad guidelines to the contractors and said, give us the best you can do according to the performance specs and trade off cost and performance and see what you come with.

We came up with two good prototypes, did enough testing, and it worked. Frankly, a rare success story in my time in Government, but it can be done.

The fourth and final point on the underlying problems that I think needs to be addressed is that there has been a steady erosion in ethical and moral standards in the way we conduct business in defense.

Politically-awarded contracts, bad contract practices, live and let live incentives for people. You do not bother contractors; that is a no-no. The revolving door—I disagree a bit with my colleague Larry. We have got to be tight on that. We have just let that one become too lucrative and too many bad things happen.

There also has been too much criticism of the public service and the people who work for it. After a while that has a real negative impact and good people disappear from the Government.

And what critics predict, when the criticism continues to go on, actually happens. We get less capable. Those are bad problems that I would relate would need some corrective action.

I conclude that due to these serious problems, the public is losing faith in our defense effort which is seen as inept or corrupt.

Draconian actions will be required to make the fixes that are needed, and I would add that no organizational changes are needed. We do not need more laws and we do not need, as I see it, more organizational changes. In fact, I would salute this committee for a tremendous job in creating the independent Chairman of the

Chiefs; that was a tremendous thing. It was the one organizational flaw of significance in the Department of Defense, and I think that has finally been corrected.

Finally, I would like to offer a seven-step proposal for the next President in terms of the corrective steps that are required.

The first is that the new President and the Secretary of Defense that he picks and the leaders of Congress together must reach an agreement on what it is going to take to clean up the Pentagon and make a public commitment to do it. That is a vital first step. Without that, nothing happens.

The second step is the new team in the Pentagon, again with Congress, is going to have to select a strategy for defense and set some priorities. For almost 10 years there has been no strategy and no priorities; it is just terrible what we have been doing.

We must also set a realistic funding level for defense for the next 3 to 5 years. That is so important at the beginning. That is one of the top constraints that you have in the Congress and the executive branch, to impose discipline on the system.

I would do a lot to improve the threat and requirement part of the process to avoid these overstated threats, so that we build weapons that are not at the edge of technology, certainly if they are not needed.

What we need on the threat is an independent assessment when new weapons come in. We just have to find a way other than the advocacy group in the service, the Air Force, the Navy or the Army, who is always going to produce extreme threats. I mean, that is understandable, but we need some independent way to check out those threats.

In the procurement system I would propose a dramatic step. I think the current procedures are so far out of control that I would propose that we throw out the procurement regulations and start again.

This is a major step. Replace the current 30,000 pages with some short, simple regs, I would like to say 100 pages or less, but something that we could live and actually run the business with, not unlike the private sector, which seems to work quite well.

I am going to propose, for that $170 billion of purchases that we make in defense every year, we break the purchases into two broad categories. One area involves items that we can buy today or within a few months from the private sector, and then the second area would be items like the weapons which are complicated and require a special set of rules.

Under these new specs, the commercially available items that we buy, we throw out all the mil specs, one, and we open up these bids to full and open competition and we operate only on sealed bid.

That is one page of the new reg for that half of the stuff that we buy each year in defense, we introduce a new operating procedure, just like the private sector does.

For the weapons, we cannot do that, we need a new system. For the weapons, I would propose that we establish—follow the prototype competition route of the F-16; you certainly have all heard that one before, that did work. And it could be done again.

Unfortunately, we have shifted back again to the paper specs. In the B-1 we have seen it time and again. Why, it is not clear, but we do it. Shifting back to the prototype competition approach where we go out with broad specs to the contractors and they come in with what they think they can do.

Under prototyping, we can see the system and test it with operators in it, in the mud or in the bad weather or whatever is needed to make sure it works. Then—and only then—do we proceed into a production line.

The contractor who wins the fly-off or the competition gets the majority of the production business, and then a second contractor team is retained to provide competition. It is in our interest as a nation to carry two competitors in all these major systems.

As the next step, we have to change the incentives that exist for Government personnel and for contractor personnel. For Government personnel, one of the things we could do to improve this whole procurement world is eliminate 50 percent of the overhead layers we have of which there are far too many in the services and in OSD.

And we can do a lot better giving more authority to the person on the firing line for Government contracts. Give him the authority he needs and when they do well, promote them, and when they do poorly, fire them, just like we do in the private sector. We need to do that.

The career force idea that Ron has proposed is another good idea that we could also implement. For contractors, I would propose to give them larger profits when they deliver something within performance specs and cost specs. That is a great deal for us and for them, and again we come out well.

Give them larger profits when they succeed, but impose severe penalties when they fail, so that they would pay the price for their mistakes.

And finally, I would say a new code of ethics needs to be imposed for the defense world. A way we can do it would be to set up a bipartisan commission of people who have been there—former people from defense and from the Congress—who could sit back and try to put together a code that would be sensible or provide the guidelines to all the people in the defense world and could be presented, as I see it, next spring so it could be acted upon by the next administration.

Those are the things that I would suggest today. I think it is going to take tremendous political will and perseverance to impose many of these. As you are well aware, these are tough. You are running up against established constituencies and folks who do not want to see change and it will be very difficult to impose many of these. But it is worth a try, I think, for the country. Thank you.

[The prepared statement of Richard A. Stubbing follows:]

Prepared Statement of Richard A. Stubbing

Mr. Chairman, the problems in defense today permeate the entire defense culture. Robert Costello, the top Pentagon acquisition executive, states that inefficiencies claim up to one-third of all defense purchases. This amounts to about $50 billion each year which defense buys no defense capability. Let me put that $50 billion in context. It equates to one-third of the federal budget deficit; it is five times the total NASA budget and it is three times the Federal budget for education.

The current problems of defense contracting are not new. They actually had their origin in the 1950's when the U.S. decided for the first time in its history to retain a large peacetime military establishment at the close of a war. At the same time, a large defense contracting industry insulated from the demands of the free market was continued. Inefficiencies developed and have been recognized for many years. In the 1980's the large growth in available funds and a managerial vacuum at the top of the Pentagon had an explosive effect on the already existing problems - a situation analogous to pouring gasoline on a small fire. The Pentagon today is, in many respects, out of control.

LET ME IDENTIFY SEVERAL UNDERLYING PROBLEMS in the world of defense contracting which have led to the long list of defense contracting scandals in recent years including overpriced spare parts, weapons that do not work (e.g. B-1, Aegis, Bradley) 'revolving door' abuses, and 55 of the top 100 defense contractors currently under investigation for illegal practices.

1. Defense contractors receive special treatment and operate in a protective cocoon. Some of the characteristics include:

-- Outsiders need not apply for large contracts. The top defense contractors in 1988 are the same as 30 years ago.

-- Major defense weapons programs are deliberately spread around among the major contractors. Competition is often only nominal.

--Considerable political interference in contract awards. Awards often go to the most financially hard pressed contractor-even though others are more qualified and have a superior bid proposal.

Boeing, for example, lost out as prime contractor on 6 major Air Force aircrafts in the last 25 years - F111, (1962), C5A (1965), B-1 (1969); KC10 (1975), M-X (1979) and C-17 (1981). In every case the Boeing proposal was highly competitive, and its past performance record was good. In each case, the winning contractor suffered from poor financial health or faced a declining business base. Boeing, by contrast, was in excellent financial shape and had a highly successful commercial business base.

-- Unsatisfactory contract performance-high costs, poor performance,-is norm on most major weapons. There are minimal penalties for failure to deliver on the contract.

-- The government minimizes the financial risks for major contractors through large progress payments, free production faculties, and flexible contract terms.

-- Unneeded weapons production lines are retained for many years (e.g. F15, A6, F14).

-- Profits are extremely high. From 1982-85, the profits of defense contractors as a return on equity were 2-3 times those of other companies in the durable goods industry. Also, a number of these defense contractors, using legal loopholes, paid no federal income tax during this four year period.

These conditions suggest a business arena far removed from the pressures of the marketplace.

2. IN DEFENSE CONTRACTING THERE ARE TOO MANY REGULATIONS, TOO MANY LAWS, TOO MANY CONSULTANTS, TOO MANY LAWYERS, AND TOO MANY POWERFUL INTERESTS OPPOSED TO CHANGE. What started in the 1950's as a relatively simple set of

rules and regulations governing defense contracting has evolved over time into a massive set of government procurement regulations which require teams of lawyers and accountants in defense and at each contractor trying to interpret what is and what is not permissible. We have lost our way in a thicket of often undecipherable bureaucracies. A major 'sea state' corrective action is needed in this area. What we DO NOT NEED is more laws and more regulations-yet that is always the corrective action taken to 'fix' the latest identified contracting problem.

3. Lack of strong 'hands-on' managerial attention to the problems which exist and to the corrective actions required to fix them. Primary responsibility for the current situation must be attributed to the civilian and military leadership defense. Congress, too, through political interference and an overemphasis on micromanagement, must also bear a share of the blame. Let me identify several key problem areas:

-- Far too much emphasis on the preparation and marketing of the budget; far too little emphasis on budget execution. Top military and civilian personnel are consumed with steering the annual defense budget through the feuding service and OSD constituencies and then through Congress. The annual budget cycle in defense starts some 21 months prior to the start of the fiscal year. By contrast, the budget cycle I experienced at Eastman Kodak lasted three months.

-- Inadequate managerial attention to the critical first steps in acquiring new weapons systems. Perhaps the most glaring problem involves the determination of the future threat and the weapon requirement which evolves from that assessment.

-- A flawed process for acquiring weapons. An overemphasis on paper studies, inadequate operational testing, too much overlap between development and production, and a ready willingness to forgive and forget when contractors fail to perform. These are all well documented problem areas.

-- A weak set of incentives to government personnel to assure good product at a reasonable cost. In fact, incentives are often perverse, with people rewarded and promoted for managerial actions that would not be tolerated in the private sector.

Let me now speak to three specific examples of major weapons that depict many of these problems and to one weapon that was highly successful.

DEFENSE CYCLEFOR MAJOR WEAPONS

THEORY	PRACTICE MAJOR FLAWS			SUCCESS
	ARMY M-I TANK	NAVY F/A 18AIRCRAFT	AIR FORCE F15 FIGHTER	AIR FORCE F16 FIGHTER
DETERMINE THREAT	OVERSTATED	OK	OVERSTATED	OK
DEFINE REQUIREMENT	GOLDPLATED TECHNOLOGY	DUAL CAPABLE AIRCRAFT	GOLDPLATED TECHNOLOGY	BROAD GUIDELINES IN-HAND TECHNOLOGY
SELECT CONTRACTOR(s)	POLITICAL INTERFERENCE	CONTRACT COST TOO LOW PERFORMANCE TOO HIGH	CONTRACT COST TOO LOW PERFORMANCE TOO HIGH	SUCCESSFUL PROTOTYPE COMPETITION
CONDUCT R+D, TESTING	INADEQUATE	INADEQUATE	INADEQUATE	INADEQUATE
COMMENCE PRODUCTION	TO SOON ENGINE PROBLEMS	FIGHTER OK; ATTACK VERSION SUBPAR	TOO SOON MAJOR ENGINE PROBLEMS	OK
PROVIDE FIELD SUPPORT	HIGH COST MAINTENANCE	OK	HIGH COST SPARES AND MODIFICATIONS	OK

The Army M-1 Abrams tank contract after an extended competition was not awarded to the contractor chosen by the Army source selection team rather, a last minute personal intervention by the Secretary of Defense resulted in a drastic change in the defined 'requirement' for the new tank. This gave a distinct advantage to the second contractor team which then was awarded the sole source contract in 1976. Inadequate operational testing led to serious performance shortfalls when the Abrams reached the operational forces. Later, production problems with the turbine engine led the Army to seek a second source to produce the engine. [Congress intervened and directed the Army not to complete the engine production.

The Navy F/A 18 Hornet had a long, tortured history in gaining acceptance within the Navy bureaucracy in the 1970's. Initially, most of the top Navy officers opposed the concept of a dual purpose fighter and attack aircraft. Eventually, the Navy accepted the program and awarded the contract. The costs doubled beyond inflation and, while the fighter version proved highly successful, the contractor could not meet the performance required for the attack version of the aircraft. The 1982 Navy Operational Test report concluded that with the Hornet replacing the A7 as the primary light attack aircraft on aircraft carriers "our current ability to engage the Soviet fleet --- will markedly diminish and the vulnerability of our [carrier] forces will be of major concern."

The Air Force F15 Eagle requirement was based on a seriously overstated Soviet threat from the MIG25 Foxbat prepared by Air Force intelligence. Years later when a Soviet defector flew a Foxbat to Japan,we found out that its actual capabilities were far less. The winning contractor team could not meet its cost targets or its performance specifications for the F15. Excessive overlap between development and production and inadequate operational testing led to major problems with operational aircraft. The contractor team received large additional sole source contracts for spare parts and design changes to get the airplane to perform as initially promised. In the 1980s the F15 Eagle production line has been sustained at ultra low production rates at an annual cost of $2 billion.

The Air Force F16 fighter proved a highly successful program. The initial requirement did not call for state of the art technology advances. Rather, loosely defined performance and cost specifications were given to each bidder. Each contractor made necessary tradeoffs and the Air Force chose two contractors to conduct a prototype fly-off competition. Both contractors produced excellent aircraft and the winning contractor delivered production aircraft to the operational forces that actually performed as advertised and at a cost reasonably close to that promised.

4. There has been a steady erosion in ethical and moral standards in defense matters. Contracts awarded for political reasons, a multitude of bad contracting practices, personnel incentives that support a 'live and let live' policy in dealings with defense contractors, and a lucrative 'revolving' door that encourages abuses all contribute to the unhealthy situation which exists today. Add to this a decade or more of political criticism of public servants and of the public service as the culprits in the current situation - and its is easy to see why good military and civilian personnel are leaving in droves.

Mr. Chairman, for all these reasons the public is losing faith in the defense effort, which they see as inept or corrupt. We must take draconian actions to change the manner in which defense conducts its business. No organizational changes are required; the establishment of an independent chairman of the JCS two years ago removed the one glaring orgainizational weakness I saw in defense. I salute this committee for its leadership in this effort. Let me close by presenting an agenda of corrective actions which could be considered as advice to the next president.

PROPOSED AGENDA FOR 1989.

1. The new president, his choice for Secretary of Defense and the defense leadership in Congress must publicly commit to greatly improved management in defense. They must be willing to support necessary, but often politically unpalatable, actions to achieve this.

2. A critical first step for the political leadership early in 1989 involves choosing a worldwide defense strategy, establishing mission and program priorities, and defining the funding levels available for our Defense effort in the next 3-5 years.

3. In determining the requirement for new weapons, use a source outside the military service to verify the reasonableness of a threat estimate.

Place great emphasis on available technology and on quantity vs. quality tradeoffs in weapons design.

4. Change the defense contracting process dramatically:

- Throw out the federal acquisition regulations which today exceed 30,000 pages. Replace them with a short, easy to understand, set of rules and regulations (say 50-100 pages). These new regulations will follow the direction in the Paperwork Reduction Act to be the least burdensome, simple, uniform, and necessary.
- Commercial specifications will replace military specifications on all common use equipment and supplies.
- For non-weapons purchases, sealed bid competition will be required. Full and-open competition will be practiced. Non-sealed bids will be considered on an exception basis.
- For weapons, broad performance and cost specifications and prototype competition will be required. Operational testing will be completed prior to production. Two contractors will be retained for production. Bids will be solicited from new companies outside defense. All spare parts will be competed. Weapons modifications programs will be done on a block change basis only and will be competed.

5. Changes in government personnel incentives:

- Eliminate at least half of the overhead layers concerned with weapons requirements and contracting. Give added discretionary authority to program managers and contracting officers and back them up when they encounter political opposition to their efforts. They must also be held fully accountable.
- Establish a career force of military and civilian program managers and contracting officers. Provide them with special training (e.g.MBA degrees) and good promotion opportunities.
- Reward military and civilian personnel with rapid promotions, public recognition and bonuses for outstanding performance in contracting and program efforts that result in cost savings to the government and in weapons that are brought in on time and that work. Penalize employers for substandard performance

6. Changes in contractor personnel incentives:

- Larger profits for successful technical and cost performance; conversely, contractors will be penalized for poor performance.
- Past performance on defense contracts will be weighed in considering new contract awards.

7. Adopt and implement a code of ethics governing acceptable and unacceptable practices for defense personnel, congressional personnel, and contractor personnel. [These could be developed by a bi-partisan commission of former executive branch, legislative branch and contractor personnel. This report should be completed by the spring of 1989 for maximum impact.

Many of these initiatives will require a stout political will and perseverance to overcome the intransigence and outright opposition from those benefitting from the current system as well as those opposed to change. The task will not be easy nor the rewards great. I can only urge that by taking these heaping doses of strong medicine, we can correct the current failings and restore the faith of our citizens in the defense contracting system.

Senator EXON. Thank you, Professor Stubbing. We will go to a 5-minute rule on questions and try to have a second round if necessary. Gentlemen, I want to thank you for your testimony. It has been tremendously interesting and helpful to this Senator.

Let me first ask a question that I guess came up as a thread through much of your testimony, but let us get back to the proposition of why is it that we do not seem to have the expertise on the Government side of all this contracting?

I know there are a lot of reasons for this situation—pay and the experience of people that work for the defense contractor and so forth and so on. But I had always felt that under a civil service system we had established career-type people that were there with the experience of a number of years who were key advisors, right-hand men and women, if you will, to the project manager of any of these contracts or contractors.

Are you indicating to us that we do not have qualified civil servants that have been there for a long time, who have had experience, who can advise the political appointees who have been assigned by the President of the United States?

Or do we simply not have that background and experience that the civil service system was supposed to provide?

Mr. FOX. I think there are two problems there. The first has to do with civil servants. I think that our training and progression in assignments of civil service personnel is inadequate in the acquisition process.

That is not to say that we do not have a number of highly qualified and very effective civil servants, but we have a very large defense procurement process, and we have far too few people who fit those qualifications.

Number two, in order for a trained, expert, career civil servant to be an effective advisor, the boss has to know, that is, the military commander of that organization or the military program manager, has to know a sufficient amount about the acquisition process and the motivation of contractors to be able to understand the advice and take action on the advice that he is provided.

At least for the past 20 years, the turnover in military personnel in the Army, Navy and, to a lesser extent, the Air Force, and the training and experience of the military personnel who have been in senior positions in the acquisition process has been far from adequate.

You also asked why is this the case; why do we have that kind of turnover? To me that is the key question because we ought to start out with the assumption that we have dedicated people. They are not people who are setting out to undermine the process. I do not believe they are.

Senator EXON. I guess my question is, if I go in a clothing store to buy a suit of clothes, I suspect that there may be a salesman who just started within the last week. But I expect that there is a tailor behind the scene.

I expect that there is a mangaer of that clothing store who knows and understands the skills of his trade and profession. I assumed that we did have that in the Pentagon. Are you telling me we do not?

Mr. Fox. Yes, sir. I think that the problem is that that kind of superstructure does not exist in the Pentagon. I think the next question one has to answer is why does it not exist? Why is it that the senior military people are not always the best trained people, the people with the experience in the acquisition process?

Senator Exon. Even if they are not the best trained people, I would assume that the experienced civil service, if we had them, would help keep them on track. But you are saying we do not have them.

Mr. Fox. I believe that the military Chiefs of Staff who control the assignments and who control the promotion system have not, over the years, appreciated the complexity and the need for the kind of expertise that you are talking about.

I think that the military positions in acquisition have often been used as alternate assignments for test pilots or ship captains or tank commanders, when what we ought to be doing is promoting people up through the acquisition process to create the kind of expertise that you find when you go into a military defense contractor organization.

Senator Exon. My time is up. Mr. Korb or Mr. Stubbing, can you add anything or give us your slant?

Dr. Korb. I would like to add two brief things here. One is that the procurement personnel within the civil service system do not have the same type of rigid entry requirements, nor do they have the same type of training that other professions within the civil service system have.

The Office of Personnel Management, as of April of this year, finally got around to "sort of" making rigid requirements for things like contract specialists, and I think we need to do much more in terms of the training and the certification of these people.

In other words, for some reason—and I had this problem when I was in office because the joint logistic commanders would come to me and I would go to OPM—they just did not think that this was that critical a field. So I think that is one thing. Not that the people in there are not good, but if we have not set the right requirements and given them the right training, then they are not going to be up to this very, very critical task.

One problem involving military people that Senator Nunn used to get after me about all the time when I was in the Pentagon, was that we were not leaving them there long enough. The services would tell you they were, but when you began to check on it, you find out that they were not. And that, I think, is a real problem.

Mr. Stubbing. I would add one point, Senator. The underlying problem, if you had to pick one is motivation. I agree partly with my colleagues. Certainly we can do with more training. The big problem is motivation. The incentive to change the way things are being done right now is lacking.

Senator Exon. Thank you. Under our early-bird rule, Senator Nunn is recognized.

Chairman Nunn. Mr. Chairman, I had to leave, so why not let the other Senators go ahead and I will trail.

Senator Exon. Thank you, Senator Nunn. Senator Levin.

Senator Levin. Thank you, Mr. Chairman. First of all, Mr. Fox, you have made a major point here of encouraging us to find a way to have a more professionalized procurement group, a separate career acquisition group, in effect.

In your book, however, you criticize Congress for micro-managing the procurement system, and indeed said the following at one point, that "Congress responded by appealing for greater professionalism by all personnel involved in the acquisition process. Understandably, morale and confidence (among the Defense Department acquisition personnel) declined further."

In other words, when we did get involved to push for the kind of professionalism which you are urging us to pursue—and I think most of us would agree with you on, by the way—the result in the Defense Department was a loss of morale. Is there any inconsistency in that?

Mr. Fox. Well, I hope there is not, Senator. I think my problem about micro-management in the book deals more with a proliferation of committees and proliferation of different voices throughout the House and Senate.

Senator Levin. Should we now be pushing by law, which is micro-managing to an extent, for greater professionalism or should we allow the Pentagon to be doing that on their own, or recommending steps on their own?

Mr. Fox. To my way of thinking, pushing for greater professionalism in the management of the acquisition process is not micromanaging. Micro-managing to me is dealing with the details of individual weapon systems, individual source selections and having hundreds of individual people in the Senate and the Congress trying to ask questions and have the Defense Department respond to them.

Senator Levin. Would you then feel we do need new laws in order to promote and require greater professionalism and career paths for people in the procurement area?

Mr. Fox. Yes, sir. I believe that we do.

Senator Levin. Then, Professor Stubbing, you say we do not need any new laws.

Mr. Stubbing. I would disagree with Mr. Fox. I do not think we would, sir. I think the urging of the Congress to get the Pentagon to clean up the situation and do what is needed through their internals is the way I would do it.

Senator Levin. You make reference to 30,000 pages of Federal acquisition regulations. I missed——

Mr. Stubbing. The show-and-tell?

Senator Levin. Was that the 30,000 pages?

Mr. Stubbing. That is the Navy equivalent. I did not count them, so I do not know, but 30,000 is the size of the Federal acquisition regs.

Senator Levin. Could you give us a guesstimate as to what proportion of that 30,000 pages is the result of law, and what is the result of internal Pentagon decision?

Mr. Stubbing. No, sir. I do not have a break. I would not know how to begin.

Senator Levin. Would you agree that a substantial proportion, maybe somewhere between 10 and 70 percent, of those regulations would be required by law?

Mr. Stubbing. Yes, sir. I have high confidence on that.

Senator LEVIN. So, in order to get down to your 50 to 100 pages, I gather, you would agree that we would have to make substantial changes in law?

Mr. STUBBING. Yes, sir. There would have to be. Part of the fix would have to be a re-look at all the laws that apply to defense, so Congress would be involved in this new process in a big way.

Senator LEVIN. So, when you say we do not need more laws, you did not mean to suggest we do not need changes?

Mr. STUBBING. No, sir. My dream would be that sitting down together we would have some summary law that really made it all work better, and that goes with the 50- to 100-page set of specs.

Senator LEVIN. I think it would be helpful to us if you would give us some specific changes in the laws that you would recommend.

Mr. STUBBING. That will take some work, but sure, I can try to do that.

Senator LEVIN. Well, a good part of that is a result of what we have done, usually to reform something, usually to correct a problem, out of good motivation.

Mr. STUBBING. Let me put some stuff together and give it to you. That is a fair challenge.

[The information follows:]

DUKE UNIVERSITY,
Durham, NC, August 8, 1988.

Senator SAM NUNN,
Chairman, Senate Armed Services Committee,
Washington, DC.

DEAR MR. CHAIRMAN: This responds to the request from Senator Levin at the hearing on August 4, 1988.

Sentor Levin asked me to identify the portions of the more than 30,000 pages of Federal Acquisition Regulations (FARs) attributable to laws imposed by Congress. He asked for specific instances of legislation which could be repealed or modified, thereby permitting sizable reductions in the size of the FARs.

The Packard Commission recommended a single, simplified procurement statute. I know the Office of Federal Procurement Policy (OFPP) has been trying to develop such a statute, with the aim of streamlining the entire process. This statute would combine key aspects of the following laws—the OFPP Act, the Small Business Act, the Federal Property and Administrative Services Act, the Armed Services Procurement Act and the Competition in Contracting Act. This proposal is still being staffed within the executive branch and holds the potential for eliminating thousands of pages in the FARs. You might wish to discuss this further with OFPP.

A second area of great potential for shrinking the FARs involves no laws but requires a commitment from the executive branch to eliminate the use of military specifications for commercially available items. Also, performance and functional specifications for new weapons should replace the current detailed military specifications on how to produce each weapon. Potential savings from these actions again range in the thousands of pages. Congress could push the next administration to implement this proposal.

These two actions, if adopted, would make a major dent in the size of the FARs. I hope the committee will push for their adoption.

If you have further questions, please call me at 919-684-3242.

Sincerely,

RICHARD A. STUBBING.

Senator LEVIN. I do not know if I have any time left. I have not gotten the magic note yet.

Let me ask one more question here, and that has to do with the issue of competition. Do you think our problems are caused by imposing too much competition on this system? Let me start with you, Dr. Korb. Larry.

Dr. KORB. Competition, I think, is excellent. Where you have problems is when you have competition for the sake of competition; when people have to meet artificially-imposed goals, because then your goal becomes getting more competition rather than getting the best buy for the taxpayer.

It is important that the Congress and the administration recognize this problem. We will compete to the extent that we can, but when you have to meet artificially imposed goals for the sake of competition I think you lose sight of your original goal.

I know that there are several instances, some of which unfortunately seem to have surfaced in this current so-called scandal, in which people, in the name of competition, went and awarded contracts that probably should not have been awarded.

Senator LEVIN. My time is up.

Senator EXON. Senator Dixon.

Senator DIXON. Thank you, Mr. Chairman.

Professor Fox, I think I will start with you, because my wife's maiden name was Fox, and there is probably some relationship by marriage here.

Did you by any chance—and I will ask all three of you this and I apologize, I have been in a Banking Committee meeting and have not heard your testimony; I am sorry I missed that and I will read it carefully—but did you read the Wall Street Journal article on the French procurement system or are you otherwise familiar with the French procurement system?

Mr. Fox. I am generally familiar with that.

Senator DIXON. I appreciate the fact that there are down sides to the type of system that they have, and I am not advocating that we change the whole structure of how we operate our procurement and acquisition system, but one of the appeals to me in that system was that this interminable competition between the various services has a response mechanism in the French system.

Because there the procurement people make those final decisions and say, "Look, we are not going to have three different missiles. Here is the missile we are going to have. You are all going to use it." And so forth, and so forth, down the line.

It frankly appeals a lot to me, because a lot of what I see in duplication, mismanagement, and a variety of things—pursuing systems like the DIVAD, you know, the Sergeant York air defense gun and other things like that—I think begins with the fact that this is part of the procurement system within a branch of the service and they pursue it assiduously, even when they know that it is not working out very well. What is your response to that?

Mr. Fox. I think that it is one of the attractive features of the French system. When people in procurement are required to look to military operations officers for their future promotions and future assignments, then I think that you have to expect the kind of problems that you describe.

Again, I am of the view that we do have motivated people, but I think one of the most dangerous things in the world is having a highly motivated person who does not know what he is doing.

Senator DIXON. That is a very sage observation. Dr. Korb, your thought on the same subject?

Dr. **Korb**. I think the problems that you mentioned, for example, like DIVAD, could have been dealt with by an active Secretary of Defense and a strong management team. There is no doubt as early as 1981, about where the problem was and the potential problems.

The real problem, I think was really one of political will, and it was not just within the Department of Defense. I think it was within the country and the Congress, because people's jobs were involved.

Senator **Dixon**. But your observation—I do not have any quarrel with anything you are saying, but your observation about the central management type of features of the French system, where it is very clear that the direct line authority for the final decisionmaking process without question is in procurement, what do you say to that?

Dr. **Korb**. I say that if you have the right people appointed to political office, you have the right system of checks and balances and would accomplish the same objective.

Senator **Dixon**. Professor Stubbing.

Mr. **Stubbing**. I would agree with Larry Korb on that one, Senator. As I see it, the services are and probably should be—there's a lot of fixing needed in the area of line authority, to continue doing the requirements and the buying of the weapons. We need to do a lot to improve the folks that are doing it.

I do not like the central procurement shop which is isolated from the services and the people who ultimately must operate and run the equipment. I just do not think that is a good idea.

Senator **Dixon**. This is a general question to any of you, or I might start again with Professor Fox—if you were going to make changes in the acquisition and procurement system now, other than the professionalism you suggested, and I think we all applaud and support that and there is more that should be done quite obviously, but if you were going to make changes internally in the system right now, as you know it now and as you view it now, what would you do?

Mr. **Fox**. The first thing that I would do is to clarify the difference between the liaison manager role and the active manager role. And to indicate that what we expect to be performed is what I described as the active management, where the Government managers share, often take a major responsibility for, cost control on a program.

I would clarify the job of the manager. I think that that is not clear today. Number two, I would try to get close to the reward and penalty system as Dick Stubbing has indicated on a number of occasions, to try to keep promotions, training, better assignments for those people who perform in accordance with the active manager role.

And I would like to find ways to pass over or fire, or not give benefits to, those people who do not respond to the job description.

Senator **Dixon**. Could I hear from the two of you as well? My time is expired.

Dr. **Korb**. I would take a page out of Dick's book where he talked about the weapons cycle and expand a little bit.

I think what we need to do is to tell industry, "Here is what we are trying to accomplish with this bomber, for example, or this fighter. Here is how much money we think we reasonably have." Have a couple of people come in and tell you what they can do, pick two to go through the development process, and, without rushing, see if they work in the field, and then pick one.

I think, for example, we could have profitably had a fly-off between the B-1 and the B-2 at some point, rather than rushing it. I think we would have all been better off if right now we had a fly-off between those two particular planes, rather than having a situation where we rushed the B-1; we got it out, so to speak, on time, and within a certain budget.

The resulting problem is the B-1 could not carry out the mission that we thought it could, and now you are faced with the situation of trying to fix the B-1 problems while simultaneously going ahead with the B-2. So I think that would-be the major change that I would make.

Mr. STUBBING. Senator, I would actually concur that on the major weapons, the idea of competition and loose specs, so that the contractors can show what they can do, as opposed to paper promises, is a critical step and I would go back again to providing proper incentive as well.

The F-15 program had tons of problems. The General in charge of that program was a colonel when he joined the F-15 team, he became a one-star in the program and then managed to misstate the facts a few times before Congress and other places, covering up as often happens, the problems that we encountered with the engine.

And, as a result of that and that kind of a performance which was known to many people, he did not get fired; he got promoted to two-star, and he got promoted to three-star, and became head of all the Air Force forces in Europe.

Well, that kind of message gets out. Let me contrast that with a fellow you certainly know, George Spanton, same program, it turned out. He blew the whistle as an auditor on a contractor that was making the engine for the F-15 down in Florida, and he whistled for some $200 million, or $300 million of overcharges. He said, that is just unfair; the labor rates they were charging were just not right. And his reward—well, he got forced into retirement, ultimately.

The signals that go out to the military and the civilian people, when you see actions like that, are the wrong signals. It says, "Hey, do not stand up." Or in the case of the general, it does not make any difference if they did not catch you on your watch, you are going to get promoted.

In the case of a civilian to stand up, that is no good. You have got to change this.

Senator DIXON. I know my time is up, but I just want to ask one more question along those lines. Is not that again, an indictment of the service acquisition system, in the nature of the system which causes each branch of the service to want to pursue assiduously, to its finite end result, the procurement policy or acquisition policy that they are involved in, again bringing me back to the one thing in the French system that does appeal to me, the fact that there is some powerful, central force that governs that.

Mr. **Stubbing**. I think the problem starts at the top. It starts with the Secretary of Defense.

Senator **Dixon**. But the Secretaries of Defense come and go, and they are political.

Mr. **Stubbing**. Change in the Pentagon emanates from the Secretary of Defense. It will never emanate from the services. And if you set up a new bureaucracy, it will have to take the Secretary of Defense to make the changes work when they run into problems. It is going to be the same thing.

Senator **Dixon**. I would like to put a statement in the record, Mr. Chairman.

[The prepared statement of Senator Dixon follows:]

PREPARED STATEMENT BY SENATOR ALAN J. DIXON

Mr. Chairman, today's hearing is the fourth we have had on the defense acquisition process. All three of our witnesses today have had actual working experiences both within the system and from the outside.

Mr. Chairman, we cannot totally legislate away greed and corruption. But we must do everything possible to correct the inherent inefficiencies of the current system and reduce the potential for abuse. The cause of national security should not be a shield for incompetence, mismanagement, corruption and cronyism.

Thank you Mr. Chairman.

Senator **Exon**. Mr. Chairman, do you have questions?

Chairman **Nunn**. Yes. I want to thank all three witnesses for being here today. I think you have already assisted us in your thinking; you have given us a lot to contemplate. We are not going to get into a big rush on this, because every time we rush something in the defense procurement area we end up creating, I think, more regulations, more problems.

I think we need to take our time and figure out where we are going for the long haul, and I hope that we can do that over the next few months.

Professor Fox, you mentioned in your testimony the need to provide clear acquisition paths for those in the field, comparable to operational career fields. You indicate that the Air Force has developed a promising acquisition career program, but the Navy and Army programs fall short of the goals.

What should be done to encourage the services to implement such programs? And a second question, how can we overcome the historic preference for field assignments as opposed to procurement assignments in the services?

Mr. **Fox**. Mr. Chairman, as your committee has in the past, I think it is important that you continue to ask people about the qualifications of the program managers and their superiors in the process. What has been their background that has qualified them to oversee giant industrial firms?

I also think, as does Dick Stubbing, that the primary action for making these changes has to be taken within the Defense Department itself, by the Office of the Secretary of Defense and, I would add, by the military chiefs of the service to whom the military and civilian people are very responsive.

What you can do in questioning a future Secretary and Deputy Secretary of Defense is indicate that the quality of the people in program management is important to translate that quality into the specific kind of requirements that I have indicated in my statement and that other people have stated as well.

We have not approached procurement or weapons acquisition as a highly professional field, and that is what the nature of that job requires. There is no easy answer. Fixed-price contracts, more regulations, those are the things that have been used in the past.

The fixed-price contract is always a quick substitute when you do not have someone in the Government who can manage the program. The problem is that the fixed-price contract reduces Government's visibility as to what is happening within the program and then, when the changes occur, the fixed-price contract ends up being counter-productive.

So I do not think that more competition, more fixed-price contracts, at least for large weapon systems, is the answer to the problem.

Chairman NUNN. Professor Stubbing, you suggested abolishing the regulations and sort of starting over. Have you thought through the transition in that process?

Mr. STUBBING. No, sir. I have thought about what can you do that is dramatic with what I see as one of the essence areas of the problem.

I have not, to be honest thought through the transition. There are times when an earthquake is required and you rebuild. I believe in this particular case we have got to make a dramatic change. It would take, obviously, a tremendous thing, but I believe for the Nation, for the long term, it is worth it.

It would require, as Senator Levin pointed out a minute ago—the Congress and the executive branch have to work closely on this one to make the changes that are required. It is regs and it is laws that have contributed to making this monster that I find worse than useless today.

Chairman NUNN. Well, I get very frustrated with the number. I do not see how anybody can be held accountable for 30,000 pages. I do not see how a program manager can possibly measure up to that.

When I first got out of law school, I worked on the House Armed Services Committee staff and my first assignment was to sit down and read, and this is in 1962, all the procurement regulations of all the services. I am probably one of the few Members of Congress who have done that, but that was 1962.

I do not know how many pages it was then. I am sure there are probably twice as many pages now. But I spent weeks and weeks and weeks reading all the procurement regulations of all the services—and each one of these volumes was very thick. So, it is impossible. I wonder how many program managers have read those 30,000 pages.

Mr. STUBBING. I think the danger, Senator, is that it is not so much that they have read them. None of them have read them. But you can find an out for almost anything or an ability to do almost anything or not do anything if you do not want to do it, somewhere in one of those pages. It becomes a reference book for special kinds of exceptions.

Chairman NUNN. Dr. Korb, what do you think of the suggestion to simply abolish and start over?

Dr. Korb. I think that we certainly have to simplify the procurement regulations. Of course, you would need some sort of transition period. If that could be done, I would support Dick's statement that we have to reduce the regs to a manageable size, and make them less complex and much more general.

And I also support the idea Dick mentioned in his testimony that you need a strong sense of ethics or ethical principles. I think one of the reasons we end up with so many rules and regulations is that we are trying to prevent these actions by people who might not act in the public good, whereas if you had a strong code of ethics or ethical principles you would need a lot less regulation.

Chairman Nunn. Let me just ask one more question. I think it was Professor Fox who, in his testimony, mentioned the importance of holding program managers accountable.

We have a whole series of revelations that have already come out about, at least allegations, about procurement fraud and so forth and so on. Each of you, in your own way, have talked about the management problems we have now. I think Dr. Korb talked about the detached Secretary of Defense and so forth, from what I have been told.

Now, as Congress takes a look and gives oversight over the next few months of this year and next year into this whole procurement area, do any of you have any procedures that you would suggest for this committee to try to instill the principle of accountability for this mess we see unfolding now?

In other words, what would you do if you were the committee itself in insisting on accountability for what we have seen and will see over the next few months?

Dr. Korb. Let me begin. I think one way in which the Congress can get involved is in the area of military promotions—you have power over the promotion process of military people. Too often people who do things or who make these mistakes are not held accountable and, in fact, get promoted. I think you need to search into this more, particularly as people get higher.

Similarly, I was very disturbed when I read about a career civil servant out at China Lake, which to me was one of the shining examples of the way to do things, who was arbitrarily transferred. I think the Congress needs to look into instances in which a person is transferred for no apparent reason or because the individual is trying to do good things. I think these are the areas in which the Congress can help to enforce accountability.

I know when I was in the Pentagon a couple of times I saw questionable promotions come across my desk, particularly of high-ranking officers. Yet when I pointed out that this individual just did this or that and asked what kind of signal it would send to the younger people, not much was done about it.

Chairman Nunn. Professor Fox.

Mr. Fox. Mr. Chairman, I think that you can be of great service when you review the costs associated with weapon systems, as you have in the past. But I think until the military services and contractors learn that the present method of operating to get higher cost does not work, until they learn that, there is not going to be any change.

Until we get to a point where a program is cancelled or cut back or a contractor's contract is cancelled for default, for failing to perform, until that happens, much of the rhetoric here will not go beyond rhetoric, whether it is rhetoric from me or from anybody else.

Somebody has to put some beef into this. Someone has to get the word across that the method of operating in the past is not going to lead to rewards in the future. I think you can do that with your appropriations and authorizations.

Chairman NUNN. Thank you. Professor Stubbing.

Mr. STUBBING. Mr. Chairman, I would agree with my colleagues that those are the things to do. The real opportunity now is that we are about to change administrations and that, as I see it, it is time for collegiality to take place between the executive branch and the legislature.

I think there is a great window here for you and the new President and the Secretary of Defense designate to agree on the key things that need to be done. What is the public commitment that we are going to make to change in the Pentagon?

What is the strategy which should be set early and the priorities and the dollars that are reasonable, so we do not go through this Mickey Mouse game of the dollars, which is the budget process all the time, and so that we set that up front and then start to impose the discipline.

The executive branch has to impose the discipline and the Congress certainly wants to make sure it is happening and keeps a watch on that. I think that could be done within the next year.

Chairman NUNN. Thank you. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman. I apologize to you, Mr. Chairman and members of the committee and members of the panel, for my absence. I happened to be conducting a hearing together with another Senator on how the Department of Defense is handling its waste problem, which is of increasing importance.

Chairman NUNN. Which problem is that, the nuclear kind?

Senator WARNER. It is not a fallout from the veto, Mr. Chairman.

I have had the privilege and pleasure of working with Dr. Korb and Professor Fox. This indeed is a very timely and fine contribution. Professor, we are glad that you have come to join us today.

Mr. FOX. Thank you, Senator.

Senator WARNER. Professor Fox, you expressed concern with the large numbers of consultants operating in the acquisition process. What steps would you recommend to bring this problem under control?

Mr. FOX. Senator, I do not believe there is a quick solution to bringing it under control. In my book I have indicated that the reason that consultants exist is because of the limited capability that exists in the military services, and because of the complexity of the acquisition process.

I am of the opinion that there is no solution to that complexity and no solution to the consultant problem until the capability is built within the Defense Department itself. Short of that, I think there will be consultants and I think many of the consultants perform a very important role in making the process work.

Senator **Warner**. Well, I share that view. Throughout this controversy I and other Members of Congress have expressed an observation—I do not know how you quantify it—that 99.9 percent of the people in Government services, out of Government service, in the private sector, are really trying to make this system work, in an honest and constructive way, in the best interests of our national defense.

But take my State of Virginia, which has a very large number of contractors. They cannot, frankly, build into their financial structure the cost to carry in-house the expertise needed, particularly in the smaller contractors, to compete in this highly competitive acquisition process. And therefore they, by necessity, are compelled to rely on consultants who are experts in the field to assist them in bidding on these contracts.

Likewise, you point out because of the system in the Pentagon of rotation among the professional military and indeed the civilian corps—which again are being sought to come back into or go to the private sector to work—it is very difficult for the Federal Government, particularly with the salary structure, to hold some of the very competent individuals in the system.

So I think your answer is a proper one. We just acknowledged that we do the best we can, but we are not going to in any way see a substantial diminution of the number of consultants. Does anyone else have a view on that question?

Dr. **Korb**. I think, Senator, you are quite right that you need consultants, and I think we have to be careful.

Senator **Warner**. In fact, were you not one at one time, to my recollection?

Dr. **Korb**. No, I worked for a company. But I think we are mixing up a lot of terms here because of this current situation. There are consultants who work for the Department of Defense; there are consultants who work for industry.

There are individual consultants. There are consulting companies. There are people who provide expertise and people who provide access. I think we have to be very careful in looking at what we are doing here. You were talking primarily about people who provide expertise, and certainly that is important.

I think we have to be careful. What is at issue are those people hired not to provide expertise but those who help you get access to people who you should have a right to see without hiring these particular individuals.

Similarly I think we need to have some sort of registry or some sort of conflict of interest standards applied to these people. Finally, if a company hires a consultant and that individual or company does something incorrect, I think the company should be held liable, as if that individual were one of their own employees.

Senator **Warner**. That is a pretty tough requirement. I would have to think about that one a little bit.

Again, I address this question to Professor Fox. In your statement you make some broad recommendations for improving the management ability of the people in the process.

Some of these changes, such as those involving military officers would have impacts beyond those parts of the Defense Department concerned with acquisition. How long do you think it would take to institutionalize your model in the Department of Defense?

Mr. Fox. I do not think it would take any longer than it takes for a Secretary of Defense and the military Chiefs of Staff to see that this committee will not look favorably on cost increases, schedule slippages, technical performance shortfalls and that you would demand professional managers, people who can motivate the industry and explain effectively the kinds of problems and deal with them.

I think that could be institutionalized quite quickly. I think you have got to find some way to get the attention of the Secretary of Defense. But I think you also have to find a way to get the attention of the military Chiefs of Staff.

Senator WARNER. Thank you, Mr. Chairman. Would you and our distinguished Senator from Michigan indulge me in one more short question?

Chairman NUNN. Certainly.

Senator WARNER. That is this question of the revolving door. The public perception is that it is highly abused. I think there are isolated incidents of abuse indeed, but on the whole the current law and regulation should be given more time to govern this almost ungovernable situation.

But Dr. Korb, you have observed it and actually were a participant.

Dr. KORB. In my testimony I mentioned that I think we ought to give the new law that went into effect in April of 1987 some time to work, because the danger as I see it is if we tighten the door too quickly, too tightly, we might not get the right people to come in in the first place.

And as we get ready to go into a new administration, I think it is important we get the best people in there to work in the Department.

Senator WARNER. Professor Stubbing, do you have a view?

Mr. STUBBING. I might disagree with Larry on that one. I think, Senator, from at least some observations of the scene that there is a lot of revolving door going on and I cannot put a percentage on it, but there is a lot of influence peddling going on.

I would be ready for a more major step with a new administration coming in, to put in some even tougher rules and regs as the new people decide to come into Government. I am willing to take the risk. I think we could try the risk with people that would come into Government.

Senator WARNER. You want to have tougher laws and regulations?

Mr. STUBBING. Yes, sir.

Senator WARNER. Are you willing to take the risk that that might adversely impact on the recruitment?

Mr. STUBBING. Yes, sir, I am willing to try that.

Senator WARNER. What type of tougher law or regulation would you implement?

Mr. STUBBING. The regs. I think the Pentagon can put them in. In concept, I would put in some tough teeth, maybe even several years that no one is allowed to go into anything related to what they were working with while they were in the Pentagon, just to see if we could get people to come into Government, recognizing that they are there to do the public service and then go back and take their chances, but it will be in something different. I think it might be worth it for the country.

Senator **Warner**. Professor Fox.

Mr. **Fox**. I would have to disagree with that, Senator.

Senator **Warner**. Let us see why we are disagreeing. We have Dr. Korb's view, we have Professor Stubbing's view.

Mr. **Fox**. I disagree with Professor Stubbing's view that we need tighter regulations. I think that we have already reached the point in regulations where we have made it extremely difficult to attract qualified people into senior positions in the acquisition management.

The laws, as I understand them, were put in place primarily to deal with people at lower levels going out and working with industry. And yet their primary effect right now, I think, is in keeping us from having the qualified managers at the higher levels.

The solution to the revolving door problem does not lie in more or tighter regulations. It is going to lie in making the acquisition business sufficiently exciting and challenging and professional and having an esprit de corps that attracts and retains people.

On the military side, we can change the system of forcing out military officers at age 45 to 50. That system, I think, is ridiculous. They have got to find a job somewhere. If I were one of those individuals, I would want to find a job where I could make the greatest contribution and I suspect that would be in the defense industry.

Senator **Warner**. Doctor, you use the word "forced out." Do you want to reconsider that word, "forced out," for the professional military?

Mr. **Fox**. No, sir. I think that the word "forced out" is the appropriate word. The retirement system and system of promotion tells people that we do not have a place for them after age 50. Now one can look at that and say that is not being forced out, but those seem like loud and clear words to me.

And if I were one of those military officers, you would not need anything stronger than that to get the word across to me. I would go out and I would find a job some place, and I would say what you have just told me is that you do not want me to stay around here. You may be even saying it stronger than that. You may say you are going to penalize me in terms of my retirement benefits if I do stay around here. I think that is the word they hear today.

Senator **Warner**. I will close with one observation. I regret to say I am becoming old enough to remember World War II, when it came upon us and we suddenly recognized that we had an officer corps that was largely over 50. And there were some very hasty actions taken to change it.

Chairman **Nunn**. Senator Levin.

Senator **Levin**. Going back to the competition issue we were discussing, Dr. Korb, do you agree that the first cause of the breakdown of this procurement system is the attempt by Congress to impose competition where it should not be imposed?

Dr. **Korb**. No, I do not.

Senator **Levin**. Professor Fox, would you agree with the statement that the first cause of the acquisition breakdown is the attempt by Congress to impose competition where it should not be imposed?

Mr. Fox. No, sir, I do not think so.

Senator Levin. Professor Stubbing.

Mr. Stubbing. No, sir.

Senator Levin. That statement was made by David Packard here last week, and created a great deal of press attention, and I also thought it was inaccurate. I think there are a lot of causes and there are places where perhaps we have imposed competition where it should not be imposed, but to call that the first cause of the breakdown, it seems to me, is really an erroneous view.

On another matter, the professionalization of the acquisition work force issue, Professor Fox, is that the same as civilianizing the work force?

Mr. Fox. No, sir.

Senator Levin. There has been a lot of confusion over that issue.

Mr. Fox. Yes, there has.

Senator Levin. Would you spend a moment telling us what the difference is between civilianizing the acquisition force and greater professionalization in the acquisition force?

Mr. Fox. Civilianizing the acquisition force means turning it into an organization for which there are no military officers. Creating a greater professionalization or creating an acquisition corps that is military and civilian, I think, means creating something along the lines of the French system we described earlier, or something closer to the Corps of Engineers, where there is a strong esprit de corps, military and civilians, in being part of that organization—where there is a career path and a set of assignments within that particular field to get promoted and to get trained.

I do not leave the corps and go out and fly airplanes or operate tanks or operate ships. I can progress and dedicate my career to becoming a more professional manager in that particular field. That is what I believe we need. I think it would be a mistake to create an all-civilian acquisition corps. I think that the military services and the military officers bring too much to lose at this point.

Senator Levin. So in your approach there is not necessarily less of a uniformed presence?

Mr. Fox. That is correct.

Senator Levin. I think, Dr. Korb, you made a reference to the incident at China Lake. One of the things we have been accused of frequently is micro-managing the Pentagon. Now you have suggested we investigate that and perhaps take corrective and reform action, to send the proper signal.

We get very different signals from people when there is a perceived or real injustice out there. Some people urge us, get on it. And at the same time people say, do not micro-manage the Pentagon.

Dr. Korb. Many times micro-management is in the eye of the beholder. That means: it is micro-management when Congress does something you do not like and when they do something you do like, it is not micro-management? I said that in response to Senator Nunn's question about this problem of accountability.

From everything I knew in this particular situation, China Lake was a model for how we ought to run our testing and development operations. In fact we talk about the China Lake experiment as a model for the way of promoting and rewarding people.

Yet here you had a situation where an individual was moved for no good reason. If, in fact, we are talking about accountability here, and if the Department does not do anything about it, then I think there are occasions when Congress ought to—it should hold a hearing and ask for an explanation, given the difference between "reality" and what actually happens.

What we needed here was a more active Secretary of Defense. There have been many Secretaries in the past, who, having heard about this situation would have demanded an explanation from the individual service. Had this occurred here Congress might not have had to get involved at all.

Senator LEVIN. The basic problem we face is how to change the system without making it worse. We recently had an experiment in tax reform that was supposed to simplify the law. And some of us think we ended up with a more complex, not a less complex law.

The truth of the matter is we are not going to send those 30,000 pages of regulations to the furnace. That is the reality. We are not going to do it. It is going to be more gradual than that.

For one thing, we have got the transition problem. For another thing, there are parts of those regulations we would immediately want to return, I presume, to the books in some way or another.

On the other hand, we all want to send most of that or a good part of it to the flames if we could at some point, in a rational way which does not create greater problems for us than we have now. So there are two issues.

One is where do we want to go, and most of us would say a different place than where we are now, probably a dramatically different place than where we are now. And the second issue is how do we get to that place. They are both major issues.

I have asked you, Professor Stubbing, if you would give us suggestions in terms of changes in law, perhaps repeal of the law, to help get to the point where we do not have 30,000 pages of regulations, and I would ask each of our other witnesses if they might do the same, become consultants, in effect, non-paid, of course, but fully disclosed.

I happen to agree with you, Dr. Korb, in terms of the disclosure, at least, of consultants' other clients. I have to tell you right now, most consultants are not required to disclose who their other clients are, and there is a built-in conflict in that situation—at least the appearance of a conflict. I should not say a conflict. There is either a conflict or the appearance of a conflict, I happen to agree with you.

But since this is a fully disclosed request for consultancy here, if all of you might furnish for the record any specific changes that you would make, no matter how radical you think we should behave, how we should end up or where we should end up, if you could give us the list of those laws that we have on the books that you would repeal or modify or what laws you would add to get us to where you think we ought to go. Thank you, Mr. Chairman.

Senator **Exon** [presiding]. Thank you very much, Senator Levin. Gentlemen, we appreciate your fine testimony and the time you have given us. I will take 5 minutes to try and wind up here.

First let me ask you about the appointment of Dr. Costello to his position. Do you think that, given the complexities you have outlined here this morning, that appointment is an important step in the right direction?

Dr. **Korb**. I think establishing the position of Under Secretary of Acquisition was a tremendous step in the right direction, because I think it is important for somebody who works directly for the Secretary of Defense to monitor the procurement process, to establish policy, to intervene by exception and whose word stands unless the service Secretaries can get to the Secretary of Defense.

I think this is very, very, very important. Unless you have someone like that on the Secretary's staff, there is no incentive for the people working on these systems to be as forthcoming as they should, because they are afraid if any of the problems get out, for example, the Secretary or the Congress may cancel the weapon system.

So I think it is very important to have somebody on the Secretary's staff with the right background, who can basically keep the Secretary and the country out of trouble on lots of these procurement problems.

Senator **Exon**. Thank you. Let me first tell you just a brief story on one minor procurement problem that I have which I think demonstrates how arcane all of these rules and regulations we go through are, and in many instances I think provide complications and, in the end, less than satisfactory equipment.

A few years ago, I had a situation where an antenna manufacturer from Nebraska had been a successful bidder for some time on the simplified whip antenna that is used on jeeps and tanks—I mean an off-the-shelf item.

A bid was put out for it. The company in Nebraska that had a good record was the second low bidder. The low bidder happened to be some name that no one had ever heard of and their address was a post office box in Philadelphia. The Department of Defense, in their wisdom, awarded the contract to the low bidder, who was only a post office box in Philadelphia.

It turned out it was one of those situations that we are running into ever more frequently, and that is that people who know the system well will put a bit on about anything, and after they get the bid then they shop around to see who they can get to manufacture the item that is trying to be purchased.

Eventually this all broke down and that particular low bidder could not deliver and did not deliver, as I remember it. You know, there must be thousands of those kinds of things happening, and they cost an awful lot of money, from redtape in the first instance, while I think we have to have competition.

I listened very carefully to your earlier statements about the fact that we did not have as much competition as we should have. You know, too much and irresponsible competition complicates the process, and it seems to me that if we can begin to revise this, we should have a list of responsible bidders, so to speak, who are the only ones that can bid on this contract.

They would have to apply and have their facilities looked at rather than their post office box. I mean, I think that thwarts the whole process. But getting down to that, that is not fraud. It is probably abuse, and it is some waste, the items that I have just satisfied.

But from your experience, gentlemen, I would like to have each of you take a shot at answering this. What percentage of our problems in defense procurement, in your opinion, are outright fraud as it appears we are running into with the most recent revelations, and what percent of it is the arcane rules, all the redtape that you have referred to Professor, and trying to go too far sometimes.

Let me give you another example. This last and best bid proposal that we have, it seems to me is almost an open invitation to some of the problems that we wrestle with. I mean, if there are six of us bidding on a contract and we make an initial bid, but then any one of us can come back in sometime later after the bids have been opened, we are almost inviting things that are not generally accepted in the bidding process.

Mr. STUBBING. I will take a quick stab at it. From my experience, I would judge the fraud part to be very low, Senator, maybe 1 percent if you want a percent. The combination of the regs, the practices within the services that create these kinds of bad situations—where you draw the line I do not know. Split it between the other two. I would not know how to draw the line between them.

Mr. FOX. I share that view, Senator. The fraud, in my experience in the Pentagon, is a miniscule part of the problem. I share all of the views that have been expressed about the regulations, except that I do not think we can do away with all of those in one sweep.

One should ask why we have the regulations in the first place. I think they are an attempt to write down in some manual every possible contingency that might arise, so that a person who is not a skilled manager in this field has something in one of those books that answers his question.

I do not think that is the way to get there. But on the other hand, if you are going to use unskilled people, it may be the closest that we can get.

Senator EXON. Larry.

Dr. KORB. I think in terms of outright fraud, it is a very, very small percentage. But one thing I think is important to point out is you do have a kind of a grey area in which people provide information or take care of each other, and that really is hard to put a handle on.

But that is something that if you had people motivated by public service and paid well, and regulated some of these consultants, that would not happen as much. I think there is another percentage caused by rules and regulations and an air of avoidance that permeates any large organization.

But the main problem in the process, in terms particularly of dollar cost and in terms of national security is rushing the development or not doing development well. There are all kinds of reasons why we rush development.

But to get back to the point I made here before, if we had it to do over again, I think we would have probably sat down and developed the B–1, developed the B–2, then had a competition, and then made a judgment.

Senator **Exon**. One last question. In World War II, we used cost-plus contracts, generally 10 percent. I am not necessarily suggesting that we go back to that but do you have any feelings on whether that might eliminate some of the problem? We also had, in World War II and sometime after that, where the Department of the Navy had some shipbuilding facilities of their own, and that was a way to measure some of the pros and cons, whether too much was being charged.

That has all been largely done away with now. We are at the mercy of the free enterprise system. As you know, we have very few bidders on ships anymore because we have a declining number of shipyards. Looking back at history, is there anything that we could look back to on procedures that we have abandoned, for one reason or another, that might be worked back in to procedures and programs that are put into place to attempt to solve some of the obvious problems that we have now?

Mr. **Stubbing**. I would suggest, in answer to that, Senator, that maybe we ought to just look not so much to history, although history is related, but to private sector and how does the private sector do it? And can we bring the private sector approach to the public sector, because truly the industry we are talking about does not operate under the regular rules.

I so not support the idea of going back to straight cost-plus contracts or directed awards to in-house Government facilities as a better answer. I would like to try and find some substitute in the world of competition.

It would never be perfect because of the special circumstances of defense, but, as I suggested earlier, for the commercially avaliable items, let us conduct sealed bids and free and open bidding and let us call that new business ethic. That is the private sector way of doing business.

For the weapons we have got to create substitutes for the private sector. I like the idea of a competitive prototype competition, with two contractors tugging and hauling to be the big winner, this gives them the right incentive to perform.

It is a good incentive and in private it works that way.

Mr. **Fox**. Senator, I agree with the comment about operating the way the private sector does. We have an important key in terms of using cost-reimbursement type contracts, cost-plus contracts for those situations where there are high-levels of uncertainty, and then managing those contracts carefully on a day-to-day basis.

I am not convinced that moving in the direction of more Government-owned ship-building facilities or Government-owned munitions facilities is any solution to the problems we are having here. I think there is a similar set of problems associated with that, and I do not think that it is going to help us.

Dr. **Korb**. I would like to add just one thing. I think on certain occasions we have to sit down and figure out how much money we have, rather than starting the other way around. In other words, we might decide at the beginning of a new administration to develop the advanced tactical aircraft, the advanced tactical fighter, whatever we are going to do, and we are going to spend a certain amount of money, and then ask the private sector, "Well, what can you give us for that amount of money?"

Then if they make that judgment, you can hold them accountable, rather than the other way. For example, I think a case history of how not to do things is with AMRAAM.

The specifications there were totally unrealistic. Lots of folks in the industry knew it. Yet lots of folks were willing to bid on it, in this case Hughes, and then they ended up not being able to do that in terms of cost.

Meanwhile, in the whole process, we did another thing we have not even talked about here. We skipped product improvement. We could have improved. We could have had a tail-controlled Sparrow to do that, while we were pushing AMRAAM and that technology out.

But I know for a fact that industry was told, "Do not dare tell the Congress that you could do that, because we have AMRAAM up here."

Senator EXON. Gentlemen, I want to thank you. You have been extremely helpful and very generous with your time. We have appreciated you taking your time to come over here and help us out. We are adjourned.

[Whereupon, at 2:23 p.m., the committee was adjourned.]

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